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March 6, 1989
NATIONAL INTERGROUP: HOW PETE LOVE WENT
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BusinessWeek
MARCH 6, 1989
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COMPUTERS

Is the Industry Maturing?

The technology is still changing rapidly, and there are plenty of opportunities left—in software, overseas markets, and powerful new products. But growth is slowing, margins are slipping, and companies are merging. An industry accustomed to high-speed growth faces a challenge for the 1990s. PAGE 68

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BOSTON'S COMPUTER MUSEUM MAY SOON BE THE PLACE FOR THE FREEWHEELING RISK-TAKERS WHO STARTED THE INDUSTRY

Cover Story

68 THE COMPUTER INDUSTRY AGES

Has middle age hit the business that turned entrepreneurs into folk heroes and upstarts into global powerhouses? Shrinking margins suggest it's so. Computer makers can no longer count on the voracious demand they're used to. So double-digit growth may be in the past—and restructuring in the future

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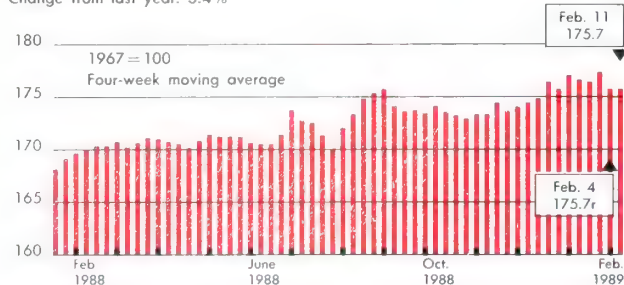
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BusinessWeek Index

PRODUCTION

Change from last week: 0.0%

Change from last year: 3.4%



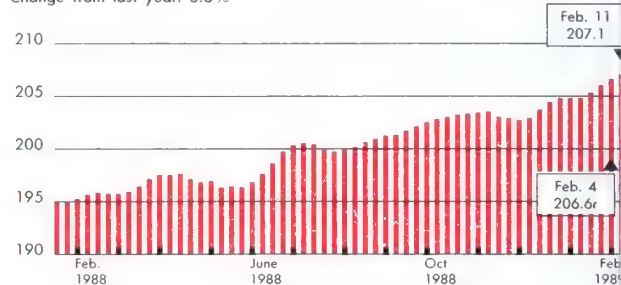
The production index was unchanged for the week ended Feb. 11. On a seasonally adjusted basis, output of electric power, rail-freight traffic, and coal increased. Production of lumber, paper, paperboard, autos, crude-oil refining, and steel declined. Truck output was unchanged from the previous week. Prior to calculation of the four-week moving average, the index jumped to 177.4, from 172.6 in the week before.

BW production index copyright 1989 by McGraw-Hill Inc.

LEADING

Change from last week: 0.2%

Change from last year: 5.8%



The leading index increased for the week ended Feb. 11, reflecting positive gains posted by individual components in earlier weeks. For the latest period, stock prices and the growth rates for M2 and real estate loans were all lower. Bond yield and changes in materials prices were the same as in the previous week. Data on business failures were unavailable. Before calculation of the four-week moving average, the index dropped to 206.7, from 207.3 in the previous week.

Leading index copyright 1989 by Center for International Business Cycle Research

PRODUCTION INDICATORS

	Latest week	Week ago	% Change year ago
STEEL (2/18) thous. of net tons	2,008	1,987 #	4.6
AUTOS (2/18) units	157,862	152,242r #	18.2
TRUCKS (2/18) units	92,064	94,196r #	7.7
ELECTRIC POWER (2/18) millions of kilowatt-hours	55,247	60,378 #	4.6
CRUDE-OIL REFINING (2/18) thous. of bbl./day	12,923	13,150 #	1.8
COAL (2/11) thous. of net tons	17,951 #	17,256	-0.9
PAPERBOARD (2/11) thous. of tons	736.5 #	752.9r	-0.7
PAPER (2/11) thous. of tons	720.0 #	753.0r	-4.8
LUMBER (2/11) millions of ft.	364.2 #	410.4	-29.1
RAIL FREIGHT (2/11) billions of ton-miles	19.1 #	18.5	4.9

Sources: American Iron & Steel Inst., Ward's Automotive Reports, Edison Electric Inst., American Petroleum Inst., Energy Dept., American Paper Inst., WWPA¹, SFPA², Association of American Railroads.

FOREIGN EXCHANGE

	Latest week	Week ago	Year ago
JAPANESE YEN (2/22)	127	126	129
GERMAN MARK (2/22)	1.84	1.84	1.69
BRITISH POUND (2/22)	1.75	1.77	1.77
FRENCH FRANC (2/22)	6.26	6.27	5.73
CANADIAN DOLLAR (2/22)	1.20	1.18	1.27
SWISS FRANC (2/22)	1.57	1.56	1.39
MEXICAN PESO (2/22) ³	2,341	2,332	2,288

Sources: Major New York banks. Currencies expressed in units per U. S. dollar, except for British pound expressed in dollars.

PRICES

	Latest week	Week ago	% Change year ago
GOLD (2/22) \$/troy oz.	386.750	381.000	-11.2
STEEL SCRAP (2/21) # 1 heavy, \$/ton	123.00	123.00	3.4
FOODSTUFFS (2/17) index, 1967 = 100	232.2	231.3	4.7
COPPER (2/18) c./lb.	134.3	139.5	20.6
ALUMINUM (2/18) c./lb.	98.5	100.8	-0.8
WHEAT (2/18) # 2 hard, \$/bu.	4.35	4.36	29.9
COTTON (2/18) strict low middling 1-1/16 in., c./lb.	54.79	55.40	-6.9

Sources: London Wed. final setting, Chicago mkt., Commodity Research Bureau, Metals Week, Kansas City mkt., Memphis mkt.

Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment.
1 = Western Wood Products Assn. 2 = Southern Forest Products Assn. 3 = Free market value NA = Not available r = revised NM = Not meaningful

LEADING INDICATORS

	Latest week	Week ago	% Change year ago
STOCK PRICES (2/17) S&P 500	294.03	296.48	1.1
CORPORATE BOND YIELD, Aaa (2/17)	9.65%	9.56%	
INDUSTRIAL MATERIALS PRICES (2/17)	102.5	102.1	
BUSINESS FAILURES (2/10)	NA	NA	
REAL ESTATE LOANS (2/8) billions	\$311.5	\$311.0r	1.1
MONEY SUPPLY, M2 (2/6) billions	\$3,079.2	\$3,081.5r	
INITIAL CLAIMS, UNEMPLOYMENT (2/4) thous.	280	299r	-1.1

Sources: Standard & Poor's, Moody's, Journal of Commerce (index: 1980 = 100), Dun & Bradstreet (failures of large companies), Federal Reserve Board, Labor Dept. CIBCR seasonally adjusts data on business failures and real estate loans.

MONTHLY ECONOMIC INDICATORS

	Latest month	Month ago	% Change year ago
CONSUMER PRICE INDEX (Jan.)	121.1	120.5	7.2
REAL GROSS WEEKLY PAY (Jan.)	\$168.21	\$167.21	-1.1
BUDGET SURPLUS OR DEFICIT (-) (Jan.) millions	\$2,806	-\$11,446	-83.1
HOUSING STARTS (Jan.) annual rate, thous.	1,693	1,568r	27.1

Sources: BLS, Treasury Dept., Commerce Dept.

MONETARY INDICATORS

	Latest week	Week ago	% Change year ago
MONEY SUPPLY, M1 (2/6)	\$787.4	\$786.7r	5.1
BANKS' BUSINESS LOANS (2/8)	309.5	306.2r	9.2
FREE RESERVES (2/8)	1,109r	462r	-6.1
NONFINANCIAL COMMERCIAL PAPER (2/8)	107.9	106.4	2.5

Sources: Federal Reserve Board (in billions, except for free reserves, which are expressed as a two-week period in millions).

MONEY MARKET RATES

	Latest week	Week ago	Year ago
FEDERAL FUNDS (2/21)	9.33%	9.29%	6.6%
PRIME (2/22)	11.00	11.00	8.5
COMMERCIAL PAPER 3-MONTH (2/22)	9.44	9.39	6.5
CERTIFICATES OF DEPOSIT 3-MONTH (2/22)	9.60	9.60	6.6
EURODOLLAR 3-MONTH (2/15)	9.58	9.34	6.6

Sources: Federal Reserve Board, First Boston

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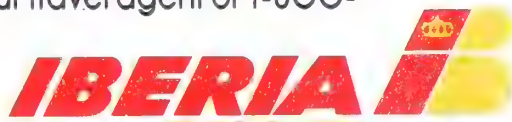


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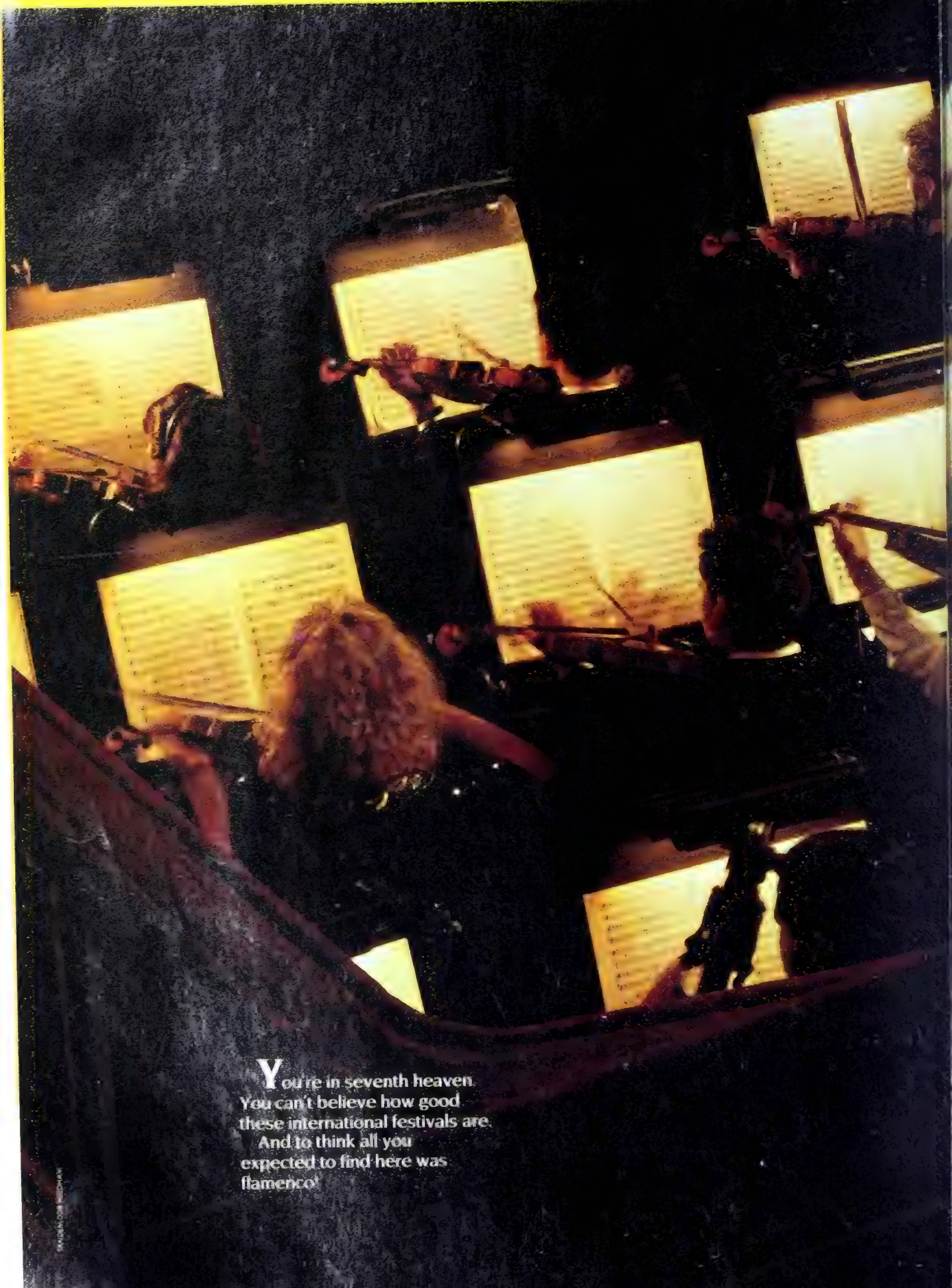
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THE CASE FOR CUTTING CAPITAL-GAINS TAXES

Your editorial "Bush hasn't proved his capital-gains case" (Editorials, Feb. 13) overlooked three salient arguments for a capital-gains tax cut.

First, companies in the embryonic stage of development do not usually get funds from the venture capital industry. Instead, fledgling companies depend heavily on equity financing from family, friends, and other informal sources of capital. Professors William E. Wetzel and John Freear of the University of New Hampshire recently surveyed 284 new companies and found that private individuals were the major source of funds for new companies raising \$500,000 or less at a time. The individuals providing startup capital for these new companies do pay capital-gains taxes and are sensitive to an increased tax rate on gains. Indexing alone will not remove the disincentives for risk-taking caused by the Tax Reform Act of 1986.

Second, our major competitors, such as West Germany and Japan, either exempt from tax [any] capital gains on portfolio equities or impose a tax at a low rate. Such policies help encourage the long-term, patient capital that tax policy experts are calling for in the U.S.

Third, a tax on capital gains increases the cost of capital to the business sector. Lower capital-gains taxes would reduce capital costs and enable U.S. companies to invest and compete more effectively.

Lower capital-gains taxes would encourage the investors to provide the seed corn necessary for the development of the IBMs and Apples of the future. Lower rates would also reduce the present unconscionable tax on phantom profits created by inflation.

Margo Thorning, Chief Economist American Council for Capital Formation Washington

ON THE WRONG TRACK ABOUT AMTRAK?

Regarding "Why Amtrak won't stop to let the taxpayer off" (The Corporation, Jan. 30): Amtrak is a national resource, and despite its remarkable ac-

complishments the U.S. has far to go in developing the superior passenger train network that other leading countries consider essential.

While other transportation subsidies have steadily grown, Amtrak's has steadily declined. In eight years of Reagan doubletalk, Amtrak is the only success story—certainly not the airlines. After getting \$25 billion of general tax funds—not user fees—the airlines show no sign of ever being "weaned from government appropriations." There is something wrong on the ground when an estimated trillion dollars is "needed" to expand airport capacity while more than a third of air travel is less than 500 miles and it takes longer to get to the plane in major cities than to make the flight.

Raymond E. Hannon
Dallas

MIXED SIGNALS ON HIGH-DEFINITION TV

Your article concerning high-definition TV, "Super television" (Cover Story, Jan. 30), focuses on whether the U.S. television manufacturing industry can rise from the dead to meet the challenge of the Japanese. Yet Federal Communications Commission standards for HDTV may make the whole manufacturing issue academic. These standards virtually guarantee that the U.S. HDTV system will be inferior, and no one will therefore be motivated to buy HDTV.

Ever since the first technical standards for TV were adopted by the FCC in the late 1940s, the commission has insisted that all technical improvements in television thereafter must be "downward compatible," that is, all new technology must be compatible with old TVs, so that no TV is ever rendered obsolete. The advantage of this is that a TV purchased in 1949 could be used in 1989. But it also means that the 1989 purchaser is buying a TV designed for a level of picture clarity possible 40 years ago.

Faced with the opportunity to break with the past, the FCC has instead decided again that no set shall ever become obsolete, and thus in effect the "super" picture quality of HDTV will have to be a lot less super. Both Europe and Japan have decided to free HDTV from these

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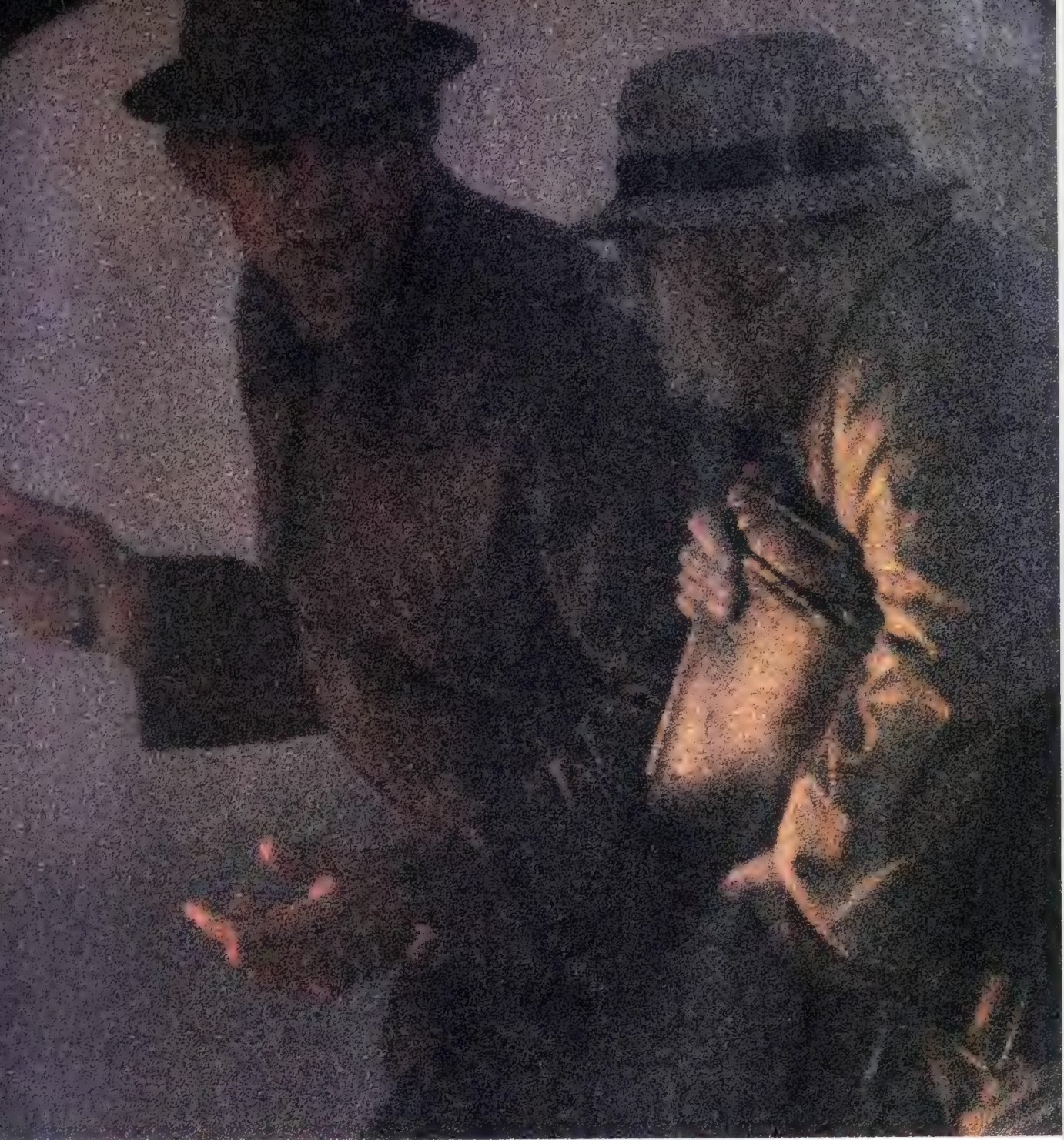
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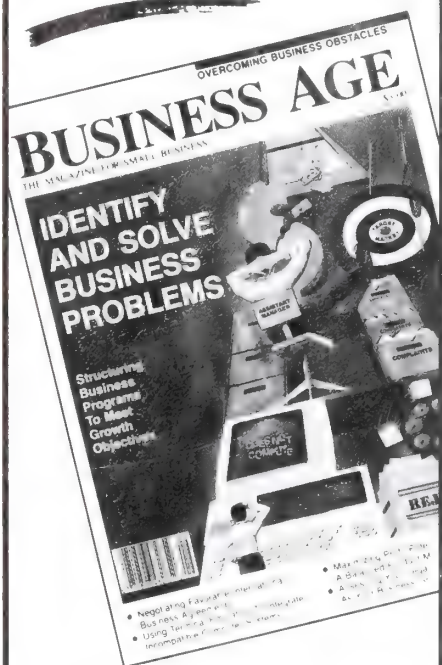
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Readers Report

technological restraints and to preserve the utility of current TVs by simulcasting in both standard and HDTV.

Why go through the exercise and expense of high-definition TV if it's really not going to be high-definition? By making a clean break with the past, Japan and Europe will be poised to take advantage of year 2000-plus technological developments, while the U.S. system will be an anachronism.

Michael Lasky
Patent Attorney
Merchant & Gould
Minneapolis

'Super television" was compelling reading. I felt that two points, however, deserved more treatment.

First, development of HDTV in a vacuum might leave us little better off than we are today as a high-tech nation. We need to develop the telecommunications that HDTV requires. I am talking about integrated services digital networks, or ISDN, for which world standards have been set by the Geneva-based International Telecommunications Union. Other countries are already building such high-speed telecommunications freeways. We have yet to begin to fashion a national policy on telecommunications in general.

Second, while HDTV and ISDN are vital to America's high-tech manufacturing prowess, the nurturing and building of our intellectual property resources is equally critical. If we succeed in building an information infrastructure America can truly tap into, we will at last be competitive in a whole new arena of information-dependent services.

John M. Eger
National Chairman
Opt In-America
Washington

HOW THE MULLAHS KEPT IN TOUCH WITH THE U.S.

Regarding "Iran is trying to shed its outlaw image" (International Outlook, Feb. 13): I was pleased to read about the "steps toward renewing normal relations." However, as an Iranian active in the trade arena after the revolution, I found your statement that "10 years after taking power, the mullahs are trying to reconstruct some of the links with the world" to be only half true.

Although Iran severed official diplomatic and economic relations with much of Western Europe and "the great satan," the unofficial channels remained open. The presence of Sweden, Italy, and West Germany was stronger than ever before, while the U.S. used indirect methods for doing business.

An incident that remains fresh in memory occurred in the summer of 1979 when the Iranian government wanted purchase several thousand tractors. Officials from a certain U.S. company traveling with Australian passport placed a bid through a member of Parliament. Although Volvo and Fiat (company I represented) were far more competitive in their prices and neither posed such ideological hypocrisy, the failure to know an "insider" cost the contract.

I'm sure the Bush Administration will do much to renew "official" links with the mullahs of Tehran. However, Reagan found during the arms-for-hostages scandal, unofficial channels, motivated solely by the dollar, will never

Shervin M. Talbot
Irvine, California

FIRST CITY BANCORP: GETTING THE NUMBERS RIGHT

In your "Investment Outlook Scoreboard" (Dec. 26/Jan. 2) erroneous numbers were carried for First City Bancorp. of Texas. The book value per share should have been \$23 rather than \$46. The -\$10.94 should have appeared not in the "1988 Analyst Estimate" column but in the adjacent "1987 Actual" column. (In fact, that -\$10.94 applies to the former First City entity, not to the present First City, which dates to the recapitalization completed in April, 1988. Finally, the \$1.95 figure carried in the column marked "1989 estimate based on 5-year trend" should instead have appeared in the "1988 Analyst Estimate" column. For your information, First City actually earned \$2.73 per share for the period Apr. 20 through Dec. 31, 1988.

James E. Dwyer
Vice-President
Public Relations
First City Bancorp. of Texas Inc.
Houston

Editor's note: We regret transposing the figures for 1987 earnings per share, 1988 analysts' estimates, and the 5-year earnings-per-share trend. As a result, the book value per share, BUSINESS WEEK does not include preferred stock in its calculations. Unlike most corporations, First City has a significant preferred position in its capital structure. That explains the difference between the two book value numbers cited by Mr. Dwyer.

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PENTAGONISTS: AN INSIDER'S VIEW OF WASTE, MANAGEMENT, AND FRAUD IN DEFENSE SPENDING

by Ernest Fitzgerald
 by John Mifflin • 344pp • \$19.95

HOW YOU ENDED UP PAYING \$7,662 FOR A COFFEEPOT

As Roman Emperor Lucius Septimius Severus lay bleeding to death at the end of a futile campaign in northern Britain, he told his two sons: "Make your soldiers rich; don't worry about anyone else."

Substitute "defense contractors" for soldiers and you have the theme of *Pentagonists*, one of the bitterest books ever written about America's militarized military Establishment. Unfortunately for the taxpayer, much of what Ernest Fitzgerald, the Serpico of the Defense Dept., has to say is close to the mark. At times an inordinately angry scribbler, at others an amusing self-portrait by an irascible whistleblower, *The Pentagonists* caps a regular career.

Fitzgerald's cost-cutting crusade became public in 1968, when he told Congress about \$2 billion in overruns on C-5A transport planes. The book begins with his subsequent firing from his position as chief of the Air Force by the Nixon administration and the long legal battle that got him reinstated at the Pentagon, where he is now top Air Force executive, albeit one who says he is isolated by

peers. Escorting the reader through quarter-century of tilting at bureaucratic windmills, the 62-year-old industrial engineer is an entertaining, though highly egocentric, guide.

Plastering the Pentagon and its civilian contractors as masters of greed striving for control of an ever-greater chunk of the peacetime economy, Fitzgerald advances a conspiracy theory that leaves few untouched. He calls officials such as former Defense Secretaries Harold Brown and James Schlesinger and former Secretary of State Henry Kissinger "indispensable front men and mouthpieces for a great, interlocked Pentagon-corporate complex that traffics in the greater part of our federal funds."

Fitzgerald never supplies evidence for that wild accusation. But when it comes to avarice at workaday levels of arms-buying, he piles it on. For starters, the taxpayer-be-damned arrogance he documents is summarized in the popular Pentagon phrase, "Execute the program." Translation: Spend all the funding appropriated for a program, no matter how bloated. That's in sharp contrast to the business world's measurement of success: achieving the greatest revenue and lowest costs possible. Indeed, early in the Carter Presidency, Defense's number-crunchers were horrified, says Fitzgerald, that spending was not keeping

so cozy that those "allowable costs" include such overhead as cocktail parties and trips for the CEO. The results can be absurd—a \$435 hammer, a \$7,622 coffee-pot, or a \$449 pair of pliers.

Fitzgerald has a surefire way to slash such prices and those of the multibillion-dollar weapons themselves. Rather than look at what a spare part or airplane did cost, he says, the military must pay only what it should cost to produce goods and services economically, plus a reasonable profit. Sensible as that idea is, it is gaining currency at the Pentagon only slowly, because the weapons community is so comfortable with often-swollen costs.

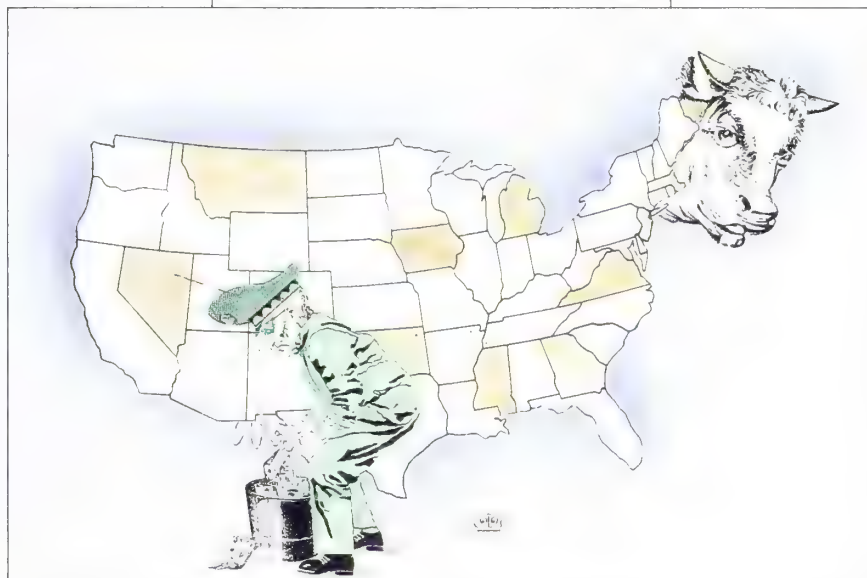
But logical pricing alone may not be enough to clean up a \$150 billion procurement system that defies rationality. Fitzgerald cites a 1987 visit to Northrop Corp., which was making guidance systems for the MX missile. So chaotic was management that it changed the design specs several times after materials were ordered. Orders and reorders swamped the purchasing department until engi-

neers bought parts themselves wherever possible, including at Radio Shack.

Tantalizing though Fitzgerald's charges are, his tendency to attack nearly every target in sight may rankle some like-minded but less zealous congressional and Pentagon officials who would like to streamline the spending machine. He won't win many friends by assailing David Packard, the chairman of Hewlett-Packard, who led a commission on defense management that President Rea-

gan, beset by procurement scandals, had to appoint four years ago. Incredibly, Fitzgerald claims that the widely admired Packard today plays a role similar to that of Alfred Krupp, Adolf Hitler's most powerful arms industrialist. He concludes: "Hitler's *wehrrwirtschaft* (roughly, 'defense economic system') was very much like our own cartel of giant defense contractors in many respects." Fitzgerald's highly debatable point is that Packard, like Krupp, is the unofficial chieftain of that system.

If that's true, Fitzgerald should spend the next few years uncovering the evidence for another book. Until then, the more rational analyses in this volume should inspire the thousands of public



MILKING THE TAXPAYER: INSIDE A \$150 BILLION PROCUREMENT SYSTEM THAT DEFIES LOGIC

up with the budget. So the Pentagon's comptroller demanded that his subordinates analyze "any unexpended balance to determine cause." Returning money to the Treasury is never an option.

The same organizational zeal allows manufacturers ridiculously high costs, claims Fitzgerald. In a typically sarcastic characterization, he calls the bureaucrats who condone such practices "cost Calvinists" because they believe in price predestination. This theology holds that a product's future costs should be based largely on the past costs allowed by the Pentagon. Thus, if the Pentagon overestimates the cost of the early version of a project, later versions compound the error. Furthermore, buyer and seller get

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Books

servants who have wondered why something can't be done about that boss who never questions the contractors' cost or the guy down the hall who signs off on quality-control inspections that haven't been done. As this book circulates through the Pentagon, Ernie Fitzgerald will be widely denounced—for the umpteenth time—for not "getting with the program." But to many readers, the book will be fresh evidence of a still fledgling brand of patriotism.

BY DAVE GRIFFITH
Washington Correspondent Griffiths covers national security for BUSINESS WEEK.

BOOK BRIEFS

AGENT OF INFLUENCE

By David Aaron
Putnam • 416pp • \$19.95

In *Agent of Influence*, the worlds of investment banking and international espionage are combined to entertain and inform. The novel's effect by David Aaron, who has studied each realm from within. Aaron was deputy assistant to the President for national security affairs from 1977 to 1981, then spent four years on Wall Street in the mergers-and-acquisition department of Oppenheimer & Co., a midsize brokerage. In 1985, he turned to writing. This is his second novel.

Unlike Tom Wolfe in *The Bonfire of the Vanities*, Aaron bases many of *Agent's* Street characters on real people. Aficionados of the deal game will recognize Jayson Lyman, the novel's protagonist, as a fictionalization of Jeffrey Beek, the founder of Oppenheimer's merger department, who was Aaron's boss. Beek now works at Drexel Burnham Lambert Inc. The book traces the serpentine path of the biggest deal in Lyman's career, advising a shadowy French mogul who is trying to take over the largest media company in the U.S. When Lyman, with the aid of an attractive female Senate staffer he meets at the Concorde, uncovers his client's real identity, he faces an ethical dilemma with dire national security implications.

Aside from its originality in casting a dealman in the lead role, Aaron's novel never rises above the conventions of the mystery-thriller. It is better on the mechanics of dealmaking than on the psychology of the dealman. Still, it's hard to put down. Aaron keeps his story perking along and invests the details with enough verisimilitude to make even the incredible seem plausible. In the end, it's almost possible to believe that a Wall Street dealman would do right by his country and his woman, even if it means forgoing a \$20 million fee. Almost.

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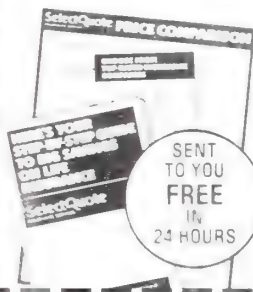
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NO RELIEF ON LATIN DEBT— WITHOUT WORLD BANK REFORM

BY PAUL CRAIG ROBERTS



The crisis in Latin America has outrun the resolution of the debt problem. If the private sector in the U.S. has to eat the debt in order to rescue the region, it should demand something in return

The much vaunted Baker plan for dealing with the Third World debt crisis has suddenly lost support, with former backers now calling for debt relief. This abrupt change in fortune for the brainchild of Secretary of State and former Treasury Secretary James A. Baker III has led to speculation that he is losing his influence.

The Baker plan sought to combine continued lending by commercial banks with a shift in emphasis toward privatization. The flight from the Baker plan is no reflection on Baker's popularity. Rather, it is a response to the specter of debt repudiation.

Much of Latin America is collapsing, economically and politically. The race is on to forgive the debt before it can be repudiated, because repudiation would shake the foundations of multilateral institutions—such as the World Bank—painstakingly constructed by the U.S. in the postwar period.

BITTER PILL. Bailing out the commercial banks' Latin American loans is no longer the issue. In diplomatic and international circles it is increasingly said that either the banks must swallow hard and write down the debt to reflect its market value or, in an effort to shift the burden ultimately to taxpayers, Western governments should buy or guarantee the debt. This all boils down to an attempt to save the World Bank's own portfolio and its AAA bond rating by lightening the burden of debt service on Latin America.

The unserviceable debt is the legacy of "development planning," an approach to economic development that concentrated investment decisions in the hands of the state. This flawed process turned over vast sums to nepotistic and corrupt governments, crowded out the private sector, and ensured that state-run enterprises would fail to return a profit sufficient to service the debt.

In place of economic progress, Latin America has acquired massive debts on the one hand and corrupt governments and irrational economies on the other. Popular discontent over the burden of debt service and the failed promise of development planning has opened running room for the far left, boding ill for stability in the region. While many in the West continue to see the debt problem as a financial issue, the lack of a viable development policy has turned the debt into an all-encompassing problem, undermining political and economic stability.

Peru, for example, has collapsed. With inflation running at 20,000% yearly, the middle class has largely disappeared. Communist terrorists control much of the countryside and bomb targets in the capital at will. The traditional leadership class is fleeing the country. Civil war

looms, and the ruling party, violently split, is stealing everything not nailed down before abandoning ship.

In Argentina, a severe power shortage and a 25% fall in the purchasing power of salaries have given the Peronist party, which launched Argentina on its downward spiral decades ago, the edge in the May presidential election. The Peronist candidate, Carlos Saúl Menem, is a proponent of a debt moratorium.

In Brazil, spiraling inflation and falling living standards have turned the upcoming elections into a contest between Marxist Luiz Ignácio "Lula" da Silva, who preaches debt repudiation and more socialism, and veteran leftist politician Leonel Brizola.

Foreign loans let government employment in Brazil balloon with political patronage, draining the budget and fueling inflation. Stories of government employees—"maharajahs"—earning huge salaries enrage the populace, but woe to the person who tries to do something about it. Recently, the governor of the state of Alagoas dismissed 15,000 unneeded officials and now faces impeachment proceedings in the state assembly.

In Mexico, after six years of declining real incomes, President Carlos Salinas de Gortari supports a workable economic program of privatization. However, the ruling party's new policy of openness in the last election has greatly strengthened the left-wing opposition party whose agenda is debt moratorium and increased socialization.

UNCLE SAM'S FAULT? Latin America has a long tradition of blaming the *Yanquis* for its economic troubles. American-sponsored development planning has hurt Latin America. The loans are the most visible symbol of this planning to the masses, who see matters simply as exploitation by *gringo* banks. Politicians who take a responsible position toward their country's foreign debt place a club in the hands of their political opponents.

The severe crisis in Latin America has outrun the resolution of the debt problem. If the private sector in the U.S., whether the banks or the taxpayers, has to eat the debt to rescue the region, multilateralism, and the World Bank's loan portfolio, it should demand something in return. Let's seize the opportunity to abandon the socialist approach to economic development that caused the debt crisis.

We can believe the World Bank is sincere about basing development on private enterprise when it sponsors an international conference to reassess the development-planning approach. The bank needs to give the boot to apologists for that failed scheme, which has set Latin America back 30 years. ■

PAUL CRAIG ROBERTS HOLDS THE JAMES E. SIMON CHAIR OF POLITICAL ECONOMY AT THE CENTER FOR STRATEGIC & INTERNATIONAL STUDIES IN WASHINGTON

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BY GENE KORETZ

CONGRESS' PAY HIKE: A LOT OF ANGER OVER VERY LITTLE MONEY

The cancellation of Congress' planned 50% pay hike may have mollified enraged taxpayers, but that raise was "a drop in the bucket" compared with what they will have to shell out for the operations of the nation's legislative body, reports the nonpartisan Tax Foundation. The research organization notes that the \$29 million pay hike was equivalent to just 7.6% of the projected rise in overall spending by Congress and its agencies during the current fiscal year—and a minuscule 1.3% of total expenditures by the legislative branch.

In line with Administration budget estimates, the legislative branch—Congress itself and such agencies as the General Accounting Office, the Library of Congress, and the Architect of the Capitol—will spend more than \$2.2 billion in fiscal 1989. That's a 21% increase over fiscal 1988, compared with inflation running at around 4.5% and a projected 7% rise in overall federal outlays.

WHY DETENTE MAY RAISE THE SAVINGS RATE

Is it possible that one of the beneficial side effects of a lessening of superpower tensions will be a rise in the long-depressed U.S. private savings rate? The idea may seem farfetched, but in recent years it has begun to capture the imaginations of a small group of economists and political scientists.

In essence, they have been exploring the hypothesis that shifts in the public's perception of the likelihood of a nuclear war may be partly responsible for slow-downs and accelerations in the rate of saving and investment in the U.S. and other economies. In a 1986 study that appeared in the *Journal of Conflict Resolution*, University of Michigan economist Joel Slemrod presented evidence that "changes in the perceived threat of nuclear war have had a significant impact on people's willingness to postpone present consumption in favor of saving during the postwar period."

Slemrod's key measure of the degree of public fear was the average annual setting-of-the-clock published in the *Bulletin of the Atomic Scientists*, which uses "minutes before midnight" to reflect the editors' opinion regarding the

imminence of a nuclear holocaust. The clock has moved as close as two minutes to midnight and as far as 12 minutes in the 1948-84 period covered by the study. Adjusting for other variables that affect savings, such as wealth and cyclical factors, Slemrod still found a significant correlation between changes in the degree of nuclear fear and shifts in the private savings rate.

Slemrod notes that since his study appeared, the minute hand on the *Bulletin* clock was adjusted back from three minutes to six minutes before midnight at the start of last year—just as the savings rate turned around and began to increase. "It has been one of the few variables that has successfully tracked the peaks and valleys of the savings rate over the past 30 years," he says.

Other researchers have followed Slemrod's lead. In an 1987 article entitled *In the Shadow of the Cloud: If There's No Tomorrow, Why Save Today?* that appeared in *Political Science Quarterly*, Yale University political scientist Bruce



THE CLOCK REFLECTS BULLETIN EDITORS' VIEWS ON THE IMMINENCE OF NUCLEAR WAR

M. Russett and congressional staffer Miles M. Lackey found evidence in public opinion polls that the savings intentions of individuals with significant disposable incomes were related to their nuclear fears. And recent research by economists Patric Hendershott of Ohio State University and Joe Peek of Boston College indicates that fear of nuclear war is one of several factors that have affected both U.S. savings rates and inflation-adjusted interest rates in recent decades. Slemrod has just completed a study covering some 20 countries that suggests that net private savings is closely correlated (negatively) with the perceived likelihood of a nuclear war.

No one, of course, believes that such considerations are decisive in determining savings behavior. "The effect appears to be small but pervasive," says Slemrod. It is also intriguing. Among major industrial countries the U.S. has one of the lowest savings rates and Japan one of the highest. And in 1988, notes Slemrod, public opinion polls in 20 countries indicated that the U.S. ranked highest in the degree of nuclear fear while Japan ranked next to the lowest.

WHITE MALES PLAY A SHRINKING ROLE IN THE WORK FORCE

Here's a puzzle. The Bureau of Labor Statistics projects that half of work force entrants between 1986 and 2000 will be women. It also projects that women will account for 63% of labor force growth during the same period. The apparent contradiction, explains the agency in its latest *Monthly Labor Review*, arises because about 50% more men than women are expected to leave the labor force over the 14-year period.

Indeed, the most interesting aspect of the BLS projections is the small part played by white nonminority men in future labor force growth. White, not Hispanic males long have been regarded as the prime group within the labor force because they tend to be more highly educated than minority men and more closely attached to the labor force than women. But the BLS says this prime working group will make up less than 10% of the 20 million people expected to be added to the labor force by the year 2000, reducing their share of the national total work force to less than 40%.

SMALL BUSINESS IS MAKING SOME BIG PLANS

To other signs of continuing economic strength, add last month's survey of owners of small businesses by the National Federation of Independent Business. Not only was small-business optimism unchanged after a surge in the quarter, reports the NFIB, but job openings reached their second-highest level during the expansion, and capital spending plans hit an all-time record level for the 16-year-old quarterly survey. Inventory investment plans were also strong, and 30% of those surveyed said they planned to raise prices during the quarter ahead—the most so inclined since the expansion began.

WITH THE ECONOMY GATHERING STEAM, PRICES ARE IN A PRESSURE COOKER

Fresh signs of the economy's vigor are emerging, but with them come new indications that upward pressures on prices are growing. Exports in December shook off their malaise, which means factory output is still getting a lift from foreign demand. Domestic demand is strong, too, but much of it is being met abroad: Imports also rose strongly in December.

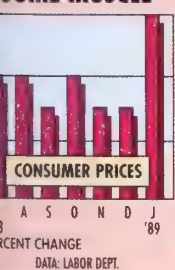
These signs of the economy's momentum are clouded by much of the business data for January. But this month's data have to be interpreted carefully, mainly because unseasonably mild weather led to a lot of business activity that usually would not have occurred. After the government applied its seasonal factors, which are designed to compensate for normal winter weakness, many of the numbers overstated the strength of the economy. Housing, employment, and retail trade are likely exaggerated.

By contrast, many of the February reports will probably look pallid. But that won't necessarily mean the economy is weakening. It probably will be best to take an average of the January and February numbers to get a more accurate reflection of reality.

INFLATION PUTS MORE STRESS ON THE FED

Still, there's no doubt that the economy is hot enough to keep an upward tilt on prices. On the heels of the big jump in producer prices in January, the consumer price index advanced a startling 0.6% (chart). Reaction in the financial markets to inflation's faster pace was surprising. After release of the data on Feb. 22, bond prices weakened, the dollar lost ground, and the Dow Jones industrial average finished the day down 42 points. Food and energy prices contributed most heavily to the overall CPI increase. But even excluding those volatile components, prices rose 0.5%. That's hot enough for the Federal Reserve to continue to raise interest rates.

INFLATION FLEXES SOME MUSCLE



The increase "disturbing" and indicated that the Fed would have to continue to restrain the economy. That

isn't what the Bush Administration wants to hear. Higher interest rates will cause trouble for the President's thrift bailout plan and will boost the government's cost of financing its budget deficit.

But for now, the Fed's first priority is to battle inflation. Consumer prices have risen 4.7% over the past 12 months. And unless the Fed tightens enough to squelch domestic demand, inflation is sure to get hotter.

EXPORTS HIT A RECORD HIGH

Strength in domestic spending is holding back improvement in the merchandise trade deficit. The trade gap made little headway at yearend, standing at \$11.9 billion—close to the \$12.2 billion for November.

Exports rose to a record high, but so did imports. That's the trade picture in a nutshell: Exports continue to do well, but our thirst for imports keeps the deficit from shrinking.

In fact, progress on trade has stalled since midyear. In the last half of 1988 the deficit shrank by only \$4 billion, to a total of \$66.8 billion. In the first half of 1988, by contrast, the deficit improved by more than \$15 billion.

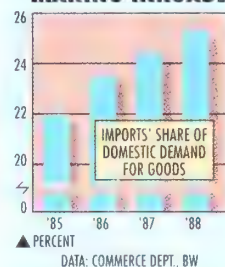
The outlook for this year shows more rough going. In December imports rose 3.3%, to a record \$41.1 billion, with greater incoming shipments of computers, cars, and industrial machinery. In addition, the combination of a robust economy and OPEC's recent price hikes worsened our oil-trade accounts. Petroleum imports in December increased in both dollar value and volume.

For all of 1988, merchandise imports increased 8.3%. That raised imports' share of the U. S. market for goods to a high of 25.3% for 1988 (chart). And since consumer and capital spending are expected to grow strongly through at least the first half of this year, the U. S. will continue to draw in more goods from overseas.

Part of the problem is that the dollar hasn't fallen evenly against all currencies. True, varying inflation rates in the U. S. and other countries play a part in determining exchange rates. But the failure of the dollar to depreciate against the currencies of many developing countries has shifted the source of our imports—not diminished them.

For example, the dollar has lost almost half of its value against the yen and the major European currencies, and this has finally begun to take a toll on imports

IMPORTS ARE STILL MAKING INROADS



from Japan and Europe, which rose just 5.4% last year. But imports from the rest of the world jumped 10.5%.

The big import gainers: the newly industrialized countries of South Korea, Singapore, Taiwan, and Hong Kong, which boosted their 1988 exports to the U.S. by more than \$5 billion, to \$66.5 billion. Not surprisingly, since early 1985 the dollar has depreciated by only about 20% against the currencies of these four NICs, as weighted by their share of U.S. imports.

But while imports keep washing ashore, exports aren't growing as fast. They rose 6%, to a new high of \$29.2 billion in December, but that increase followed two months of declines. On a year-over-year basis, merchandise exports grew by 22% last quarter, down from a 31% rate of growth in the first quarter of last year.

One factor that will hold down export growth this year is the already-high utilization of capacity in some industries. The manufacturing industries with the fastest export growth in 1988—chemicals, steel, and nonferrous metals—have operating rates around 90%. Clearly, many exporters will be hard-pressed to increase shipments abroad—even when the demand is there.

Another major source of exports—the farm sector—is suffering from last summer's drought. Agricultural exports fell at an annual rate of 33.4% in the fourth quarter. Domestic inventories of many farm products remain low, and snow and rainfall have been below normal for some parts of the nation so far this year (page 24). So agriculture may not add much to export growth in 1989.

If export growth slows while our appetite for imports remains insatiable, the trade deficit isn't likely to get any better in 1989. That would be a drag on the economy.

HOUSING IS ON SHAKIER GROUND

Housing probably won't be a source of economic strength this year, either. Home construction's surprisingly strong performance at the end of last year continued into 1989, but not without a lot of help from January's

mild weather. The outlook for housing for the rest of the year is not as bright, particularly because the latest rise in interest rates should be followed by further hikes later on in 1989.

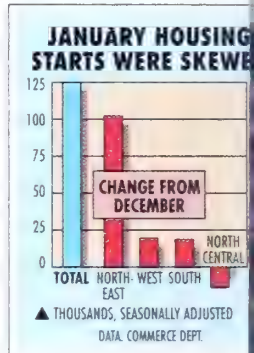
Housing starts jumped 8% in January, to an annual rate of 1.69 million, compared with a 1.57 million pace in December. But two signs give the tip-off that the January numbers were distorted. First, contractors didn't rush to sign up for new building permits. Permits actually fell 2.7%, to 1.52 million. Second, more than 80% of January starts showed up in the Northeast, where weather conditions were unusually tame (chart).

New construction strengthened at yearend, mainly because 30-year fixed mortgage rates dipped from a U.S. average of about 10.7% in August to about 10.1% in November, a drop of more than half a percentage point.

Starts averaged 1.56 million during the fourth quarter, up from 1.49 million for all of last year. But since November, interest rates have been moving up. The rate on 30-year fixed mortgages hit 11% in January and was hovering close to that in mid-February.

That's why the January level of housing starts is unlikely to hold in coming months. Starts, unadjusted for seasonal behavior, actually rose in January—something they almost never do. Seasonally adjusted starts in February are likely to post a sharp decline, if only because of the return to more normal weather.

Without housing and without much improvement in the trade deficit, the economy may begin to show signs of slower growth in the second half of the year. And that could become even more pronounced as inflationary pressures force the Fed to raise interest rates further.



THE WEEK AHEAD

GROSS NATIONAL PRODUCT (REVISION)

Tuesday, Feb. 28, 8:30 a.m.

Economic growth in the fourth quarter will probably be revised to an annual rate of 2.5%, up from the original estimate of 2%. Improvement in net exports, faster inventory accumulation, and higher growth in consumer spending contributed to the overall revision.

CONSTRUCTION SPENDING

Wednesday, Mar. 1, 10 a.m.

Warm weather most likely caused construction spending to jump 2.5% in January, the same increase as in December. Building activity remains a surprise contributor to economic growth. Despite high mortgage and vacancy rates, Janu-

ary's building activity should be about 9.6% above its year-ago level.

PERSONAL INCOME

Wednesday, Mar. 1, 10 a.m.

Personal income probably rose 0.8% in January, following a 0.9% advance in December. Wages and salaries increased sharply in January. Consumer spending likely edged up only 0.3% after rising 0.9% in December. A 15% drop in new car sales offset gains in other spending.

NEW SINGLE-FAMILY HOME SALES

Thursday, Mar. 2, 10 a.m.

New homes most likely sold at an annual rate of 700,000 in January. Warm weather was a big factor in the increase, which is probably unsustainable. The

sales rate in December was just 669,000.

LEADING INDICATORS

Friday, Mar. 3, 8:30 a.m.

The Commerce Dept. has revamped its index of leading indicators. The new index for January will probably show a 0.5% increase. Economists are wondering whether the new index will show an upsurge in economic growth. Growth in the old index had been weak since July.

FACTORY INVENTORIES

Friday, Mar. 3, 10 a.m.

Manufacturers probably increased their inventories by 0.6% in January. Stocks had grown 0.7% in December. With sales strong, factory inventories show signs of unwanted accumulation.

*The difference between a shattered windshield
and a shattered life.*



November 17, 1986, the car in which Tara Meyer was riding was in an accident. Unfortunately, she wasn't wearing her seat belt. So like 150,000 other Americans each year, her head hit and shattered the windshield.

But unlike many of the others, Tara suffered no facial cuts or lacerations.

The difference?

A new idea developed by a group of DuPont engineers. They believed that a thin layer of plastic along the inside of the windshield would keep the razor-sharp, shattered glass on the outside—away from the occupants.

Their idea helped make more than just a safer windshield... it made a difference.

And that's something we try to do in everything we do.

At DuPont, we make the things that make a difference.

Better things for better living.



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MOTOR CITY MADNESS

GM LEADS DETROIT TOWARD A COSTLY NEW CAR GLUT

Roger B. Smith takes solace in a recent trip to the supermarket. "When I saw that every cereal manufacturer already has the rebate printed right on the box," the General Motors Corp. chief said, "I thought maybe the automobile business isn't so bad."

Not yet. But by overproducing in the face of expected weaker sales, GM is leading the auto industry back into a blizzard of rebate and financing incentives. Some dealers think carmakers' come-ons are just the ticket. "We need something to stir up the market," contends James A. Hoffer, general sales manager at Jordan Motors Inc. in Mishawaka, Ind. But in so doing, GM will backslide in its bid to wean U.S. car buyers away from the costly incentives.

HOLDING THE LINE. At one point that effort seemed to be bearing fruit. Last summer, for the first time since 1984, Detroit managed to avoid the across-the-board 2.9% or 1.9% financing incentives that had become as much a fixture in consumers' psyches as back-to-school promotions by retailers. How did the carmakers do it? By keeping inventories in line with sales. GM, which had been the most flagrant overproducer in recent years, learned self-control. Even as stronger-than-expected demand helped it sell 2.3% more cars in 1988, its dealers' month-end inventories averaged 807,000 cars, 16% fewer than in 1987 and 20% fewer than in 1986. Month-end stocks never topped 886,000 cars, after passing 1 million units five times in 1987.

True, carmakers still spent plenty on incentives. Ford Motor Co., in fact, dished out \$100 a vehicle more on incentives in 1988 than in 1987. But Ford and the rest of the industry spread the rebates out over the entire year and focused on specific, slow-moving models. As a result, Detroit avoided the sort of blockbuster giveaways that only remind customers to put off their next purchase until rebates return. Auto makers hoped this year would follow that pattern, despite a consensus that sales will ease to

about 15 million cars and trucks from the 15.8 million sold in 1988. Says a hopeful Lee A. Iacocca, chairman of Chrysler Corp.: "I would like to hold market share without adding another couple hundred million dollars every quarter to incentives and price reductions."

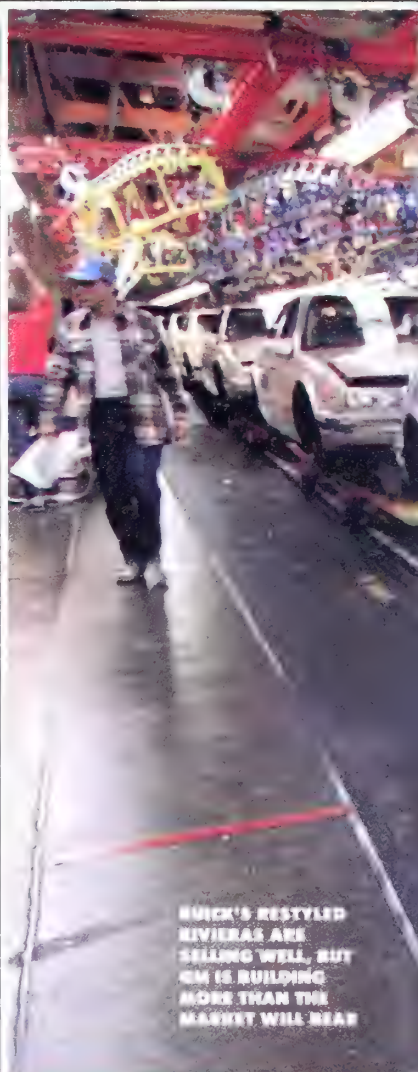
Iacocca won't get his wish. Chrysler is scheduling production at its factories in line with the sales slowdown (charts). Ford is overbuilding, but the recent idling of its Hermosillo (Mexico) plant proves that it's willing to cut output if needed. But GM is opening the spigot. Its rationale: Higher volume more than offsets the cost of added incentives.

GM's ambitious schedules call for its plants to build nearly 17% more cars in the first quarter than they did a year earlier. Its inventories at the end of January stood at 892,000 cars—more than at the end of any month last year. That was equivalent to 95 days' supply, up from 73 days' supply at the end of December and well above the 86 days that is normal for the industry in January. If GM sticks to its production schedule, warns Ronald A. Glantz, auto analyst at Montgomery Securities, the industry will end the second quarter with its highest stocks since the summer of 1979.

Some of the bulge on the car lots isn't surprising. GM has a 156-day supply of the Chevrolet Corvette, but the sports car rarely sells well in the dead of winter. And the low-volume Buick Reatta and Cadillac Allante have been in chronic oversupply since their introduction.

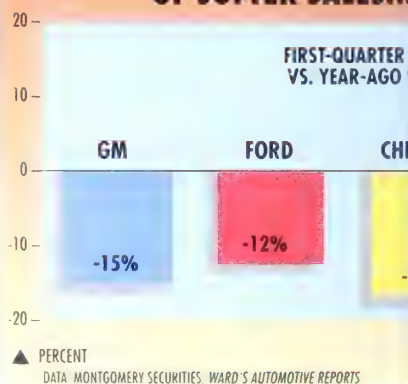
The Buick Riviera is another matter. Sales are up 81% since it was restyled last October, yet stockpiles have climbed to 111 days' supply. In all, 23 GM models had more than 100 days' supply at the end of January. Says Glantz: "They're in trouble pretty much across the board."

Unlike last year, Detroit won't be rescued by an unforeseen sales surge. After six years of robust sales, the industry is due for a slowdown. Buyers are keeping their cars longer: 1988 Chevrolet buyers, for example, expected to keep



BUICK'S RESTYLED RIVIERAS ARE SELLING WELL, BUT GM IS BUILDING MORE THAN THE MARKET WILL BEAR

DESPITE FORECASTS OF SOFTER SALES...



their cars 5.1 years, up from 4.6 years in 1986, according to J. D. Power & Associates, an Agoura Hills (Calif.) market research firm. And interest rates are headed up, while household installment credit outstanding last year crept up to decade-high 19.2% of disposable income. At best, car sales may hold their own. Excluding a late-December sales surge sparked in part by fleet purchases, passenger-car unit sales have held relative

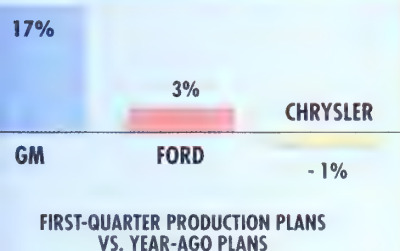


borrowers are subject to greater scrutiny. "We're not concerned about taking serious losses," says William J. Lovejoy, group vice-president for marketing at General Motors Acceptance Corp. Yet GMAC is test-marketing a direct-mail offer to consumers to take home-equity loans to buy a car, one of a number of moves to lower its risk.

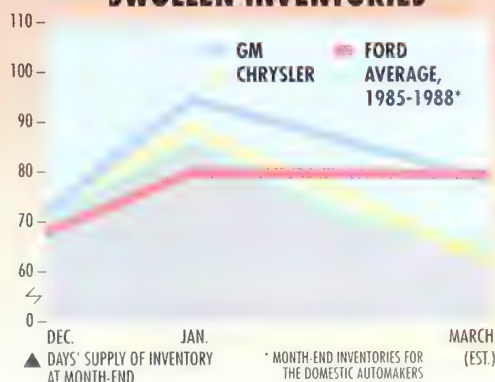
PROMOTIONS. Nonetheless, GMAC's marching orders remain the same: Get shoppers to buy cars. GM set aside an estimated \$1.5 billion in the fourth quarter for future incentives. Montgomery's Glantz figures that's equivalent to \$972 for every car and truck GM will build in the first quarter vs. \$499 a unit a year ago. In other words, GM is getting ready to deal.

GM's current incentives expire mostly on Feb. 28 and Mar. 3. The Cadillac division has called a meeting for some of its dealers in Cincinnati on Mar. 2. "A spring meeting usually means some sort of promotion," notes Donald E. Massey, owner of Don Massey Cadillac Inc. in Plymouth, Mich. The new incentives will likely combine both lower interest rates, particularly for shorter-term loans, and rebates. They'll also be targeted at specific buyers. Now, for instance, through a coupon in *Modern Maturity* magazine, the Buick division is offering \$300 off to buyers in the Southeast who are over 50 years old. And when GM acts, others will follow. As Ross H. Roberts, general manager at Ford's Lincoln-Mercury Div., puts it: "We'll have to make sure

...GM IS STEPPING UP OUTPUT...



...THE RESULT: SWOLLEN INVENTORIES



ly for about the past four months. thus eventually must cut back its ut, probably in the second quarter. a so, GM's dealers may take it on selves to thin out their car lots—by ng back their orders. Dealers are up rms over a pending notice from the aker that it will no longer grant a carryover allowance" on select 1989 els when the 1990s are unveiled. The vance, effectively a rebate to deal-

ers, helped them move unsold last-year models. In a blistering telegram to Smith and GM President Robert C. Stempel, National Automobile Dealers Assn. President Ron B. Tonkin denounced the move as "an unconscionable act." Adds Tonkin: "I think it could affect third-quarter ordering very drastically."

What's more, tighter credit could keep some shoppers away. With GM's repossession up 12% in 1988, to \$343 million,

our dealers remain competitive."

By trimming production plans to what dealers want to buy and by luring customers with fresh incentives, Motown could be able to work its stockpiles down to reasonable levels. But at the moment, Roger Smith is doing nothing to keep from having to paint the rebate right on the car door at the factory.

By James B. Treece, with David Woodruff, in Detroit



KANSAS FARMER ARMSTRONG: WITH NO SNOW COVER, HIS WINTER WHEAT IS LIKELY TO DIE

WINTERTIME—AND THE FARMERS AREN'T EASY

Drought and wild temperatures already menace this summer's crops

Think of winter on the Great Plains...visions of snow-covered fields and white-all-over farmhouses. Think again. It's not white that John Junior Armstrong sees around his Muscotah (Kan.) farm. He's eyeing drought. Laments Armstrong: "I'm in one of the driest counties in the state."

Farmers across Kansas are fretting that their hard, red winter wheat, the state's major crop, may be lying in the soil, dead, the victim of too little moisture and too wild temperatures. Nor is Kansas alone in suffering winter's wrath: There's flooding east of the Mississippi and a big chill in California.

Last summer's drought helped to push long-quiescent food prices up 4% in 1988. This year, with inflation suddenly having become an increasing source of anxiety and folks nationwide wondering what gives with the weather, there's a keen interest in the coming growing season. Do drought, shriveled crops, and sprouting prices lie ahead?

FALSE SUMMER. Not to worry, say the weathermen. Despite the patches of problems in areas beset by weird weather, the Agriculture Dept.'s chief meteorologist, Norton D. Strommen, is optimistic. "The outlook for agricultural production going into the planting season is encouraging," he says, "particu-

larly compared with where we were last fall." One especially good sign: In some areas, there has been a full recharge of soil moisture.

Of course, that's little solace to the farmers in Kansas. There, "winter kill" occurs when the snow cover is so thin that the wheat crop goes unprotected when the "Siberian express" barrels in with subzero temperatures. This year, the weather in parts of Kansas, Oklahoma, and Texas wrought unusual havoc. "On Feb. 1," Armstrong recalls, "we were up to 72 degrees. The wheat was starting to come out. Within 24 hours, it had dropped to seven below zero."

Even if the winter wheat recovers

from the frost, continued dryness could doom it. Ed Johannsen, a farmer in Little River, Kan., planted 600 acres of winter wheat. He's anticipating a loss between 30% and 50% if springtime brings little rain. "If it's all gone," Johannsen says, "I will lose between \$100 and \$200 an acre"—a total of \$60,000 to \$120,000.

Although only one crop, winter wheat is of no small importance. Planted in October and harvested in June and July, it represents 80% of the nation's wheat crop, a key ingredient in food staples such as bread. Even food companies are worried. Says John Ferris, senior vice president of finance at the Minneapolis-based Super Valu Stores Inc., a major food distributor: "If we don't get adequate moisture in the spring, there's no question that prices will be affected." Further reflecting the fears is the futures market. The nearby contract for winter wheat now trades around \$4.30 a bushel—not far off the \$4.32 high during the drought last summer.

Winter wheat is not the only concern. Cold weather will likely push up prices on fruits and vegetables, too. Below-zero weather in the Grand Valley farming country of Colorado has done serious damage there. "No apricots, sweet cherries, or peaches," observes Max L. Noland, a farmer in Palisade.

PUMPING COSTS. It's worse yet in California, which is suffering a double whammy of cold and drought. The state's oranges, lemons, and avocados have fallen victim to frigid temperatures. Farmer Donald J. Laux, who supplies Sunkist Growers Inc. with oranges and lemons from his 4,000-acre ranch in the San Joaquin Valley town of Porterville, reckons he lost a quarter of his orange crop and three-fourths of his lemons.

Meanwhile, water levels in the state's reservoirs are 65% of normal. U.S. Bureau of Reclamation officials are warning California farmers that their water allocations may be cut by 50% unless rains come. That would be the first time in memory that the bureau's Central Valley Project has taken such a step. "This year the drought will have a pretty severe effect," says William L. DeBois, water expert for the California Farm Bureau Federation. That's because pumping groundwater costs a lot more than simply drawing it from government irrigation projects. For example, one Sacramento County farmer now pumps water from 140 feet below the surface, which costs \$25 an acre-foot, compared with \$3 an acre-foot to get water only 10 feet below ground.

Rain also is the watchword for harvesters of corn, soybeans, and spring wheat. Because last year's drought d-



cally lowered crop stockpiles (chart) sucked moisture out of the farm-subsoil, another drought year would be devastating. For example, last year's corn crop of 4.9 billion bushels was 30% lower than the previous year's. That left lower carryover supplies for this season: Current stocks of corn are less than half what they were one year ago. Says Sherman L. Levin, a Chicago business consultant: "The stocks are low—provided the next growing

season has at least a normal crop."

History offers some comfort. "Never have you had two severe droughts in a row," notes Steve Freed, grain analyst with Dean Witter Reynolds Inc. If history repeats itself and the drought doesn't, inflation watchers will be joining farmers in a huge sigh of relief.

By Kathleen A. Behof in Chicago, with Robert D. Hof in San Francisco and Sandra D. Atchison in Denver, and bureau reports

ADMINISTRATION

WANTED: A FEW GOOD LEADERS FOR THE BUSH TEAM

High-level vacancies are severely handicapping the new Administration

A treaty to ban all chemical weapons is high on President Bush's foreign policy agenda. So naturally, members of the Senate Foreign Relations Committee were curious about the Administration's plans during a re-briefing by William F. Burns, the outgoing head of the Arms Control & Disarmament Agency. What was the President's policy on sanctions against countries that produce chemical weapons? Burns's response, as characterized by a participant: "Beats me."

That's an answer an inquisitive congress may be hearing a lot. For five weeks in office, the new Administration remains mysteriously invisible. The White House has filled only a handful of sub-Cabinet jobs—the Under Secretaries and Assistant Secretaries—who run the government. Though most of the Cabinet has been confirmed, the rest of the Administration is a hodgepodge of "acting" officials, Reagan holdovers, and future nominees working as consultants or temporaries. And the delays are starting to affect decision-making, from nuclear-arms strategy to Central American policy. "Not optimum situation," sighs one official lapsing into Bushspeak.

Even when it comes to such routine matters as congressional hearings, the Administration finds itself severely handicapped. "We don't have a lot of people below the Cabinet level prepared to testify," complains one White House aide. "The committees are getting people who are left over from the Reagan Administration, and they're not in a position to talk about future policy." Fingerprinters are out in force. Some White House officials blame the FBI,

which conducts background checks, for taking too long. Cabinet officials blame a green White House staff for the personnel snafu, with many of the daggers aimed at personnel chief Chase Untermeyer. Bush himself may have contributed to the mess by demanding tougher ethical scrutiny of nominees and in some



cases slowing down the hiring process in an attempt to recruit more women and minorities.

As a result, a Bush Administration that vowed to "hit the ground running" is wasting precious time. "If he can't get his appointments in place before the honeymoon is over, the President loses a tremendous policy advantage," says Howard McCurdy, a public administration professor at American University.

With "vacancy" signs up all over town, policymaking is suffering. The State Dept. was taken by surprise on Feb. 14 when five Central American

leaders agreed to disarm Nicaraguan rebels. The lapse was blamed in part on the absence of key policy aides. "We would like to have senior State Dept. officials address important foreign policy issues," says Senate Foreign Relations Chairman Claiborne Pell (D-R.I.), "but that has not been possible."

The Pentagon's problems are worse. All nominations are on hold pending a decision on former Senator John G. Tower's appointment as Defense Secretary. The Pentagon missed a Feb. 15 congressional deadline for deciding between the competing MX and Midgetman ground-based strategic missiles. More important, top-level vacancies make it difficult for officials to flesh out a 1990 military budget that, at best, will grow only at the rate of inflation.

NO PLACEMENT. Several key agencies will be leaderless during critical periods. Eastern Airlines Inc. and its unions are heading for a showdown that has broad implications for the national transportation system (page 26). But Federal Aviation Administrator T. Alan McArtor left office on Feb. 17 without a successor. Transportation Secretary Samuel K. Skinner would like to appoint a special assistant for aviation, but no one has been named. And Labor Secretary Elizabeth H. Dole, whose specialty is jobs, hasn't filled any of the big ones on her team.

Officials throughout the government are losing patience with the slow pace of nominations. "We're having trouble getting the attention of the senior White House staff for our appointments," says a top aide at the Justice Dept. Even Commerce Secretary Robert A. Mosbacher, a Bush intimate, has found the going rough. He submitted his recommendations, only to discover that the White House had its own candidates for several jobs. The resulting delay angered Mosbacher and led him to launch a couple of well-aimed torpedoes at Untermeyer's operation.

So far, the White House is reacting stoically to the staffing muddle. "Everybody wishes it was faster, but they realize why it has to be this way," says a White House aide. "There are very few mistakes of the kind that a cursory background check would have produced."

Caution is a hallmark of the Bush Presidency. But staffing delays could deprive Bush of his opportunity to seize the national agenda. "Congressional Democrats won't wait for us to get our act together," frets a White House official. "And the world won't wait either."

By Richard Fly, with Bill Javetski, in Washington

EASTERN'S LABOR MESS MAY LAND IN BUSH'S LAP

The President could turn to an emergency mediation board for help

The struggle between Eastern Air Lines Inc. and its unions has become one of the nastiest labor battles of the decade. Now it's spilling over into the political arena, where it's fast becoming a messy problem for both President Bush and Congress. Like the 1981 face-off between Ronald Reagan and the air traffic controllers, the Eastern imbroglio confronts Bush with a critical first test in dealing with organized labor.

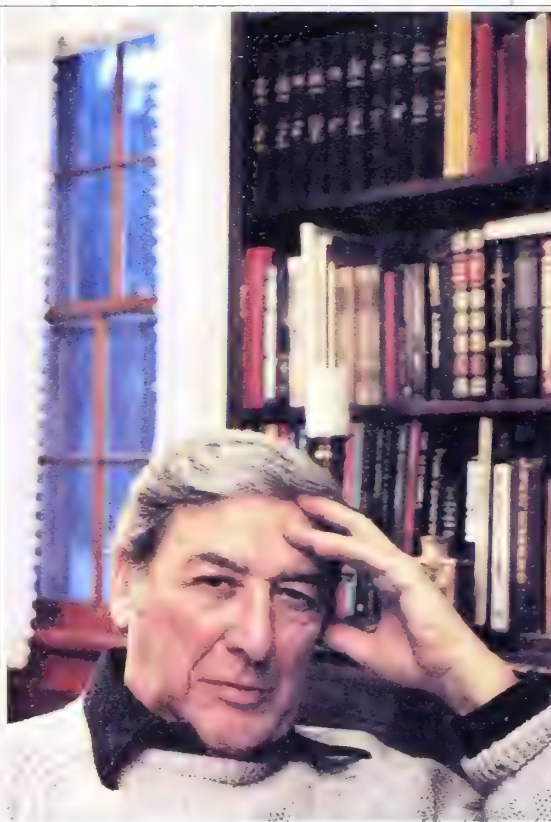
Eastern's woes are being thrust onto center stage by the National Mediation Board (NMB). In early February the NMB said that if a settlement wasn't reached by Mar. 4, Eastern's machinists could strike and the carrier could impose the wage cuts of up to 36% it has been after since Texas Air Chairman Frank Lorenzo bought Eastern three years ago. The NMB on Feb. 22 initiated last-ditch settlement talks. But board sources say the NMB is set on Feb. 24 to ask Bush to appoint a three-person emergency board to mediate the dispute. If Bush agrees, a showdown will be delayed for 60 more days while the board devises a settlement plan. If either side rejects the plan, Congress could impose a deal.

FLY ON? The possibility of intervention has already sparked intense political maneuvering. Lorenzo is lobbying hard to keep the White House out of it. The reason: Texas Air Corp. officials hope they can finally break the International Association of Machinists (IAM) by flying through a strike. What the officials know is that Texas Air, with its other carrier, Continental Airlines Inc., also in the red, can't let the fight go on. Continental lost \$315.5 million in 1988 and may drop \$50 million in the first quarter.

For its part, the IAM is pushing for an emergency board by trying to show that it can disrupt national air and rail traffic in a strike. "If Bush agrees to set up a board, Lorenzo will be in real trouble," says one source who wants Bush to appoint a board. "If Bush doesn't, he could have a mess on his hands."

The establishment of an emergency board would be highly unusual. The NMB can recommend one when it believes

that a rail or airline strike would cause national transportation problems, but it hasn't done so in an airline dispute since 1966. The NMB's chairman, Walter C. Wallace, decided to act now because he found that the IAM could cause severe problems. IAM members work at four big



NMB CHAIRMAN WALLACE: INVITING INTERVENTION

airlines besides Eastern, and while its contracts all have no-strike clauses, the NMB's lawyers think the union could still legally strike two of the airlines.

More important is what the thousands of IAM railway workers could do. NMB sources claim that the IAM could wreak havoc on most of the East Coast's rail

If the IAM strikes at Eastern, thousands of its railway workers might follow, halting East Coast trains

lines. In addition to likely grounding Eastern shuttle, the IAM could stop Conrail and Amtrak. This in turn could disrupt traffic on New Jersey Transit and the Long Island RR.

The Administration began to grapple with a response on Feb. 15, when White House Counsel C. Boyden Gray, who will advise Bush on the issue, met with officials from the Labor Dept. and Federal Aviation Administration. White House personnel department began to scrutinize Wallace's candidacy for an emergency board, including Samuel R. Pierce Jr., the former Housing and Urban Development Secretary. Pierce, who would be the board's chairman, is an old Wallace pal.

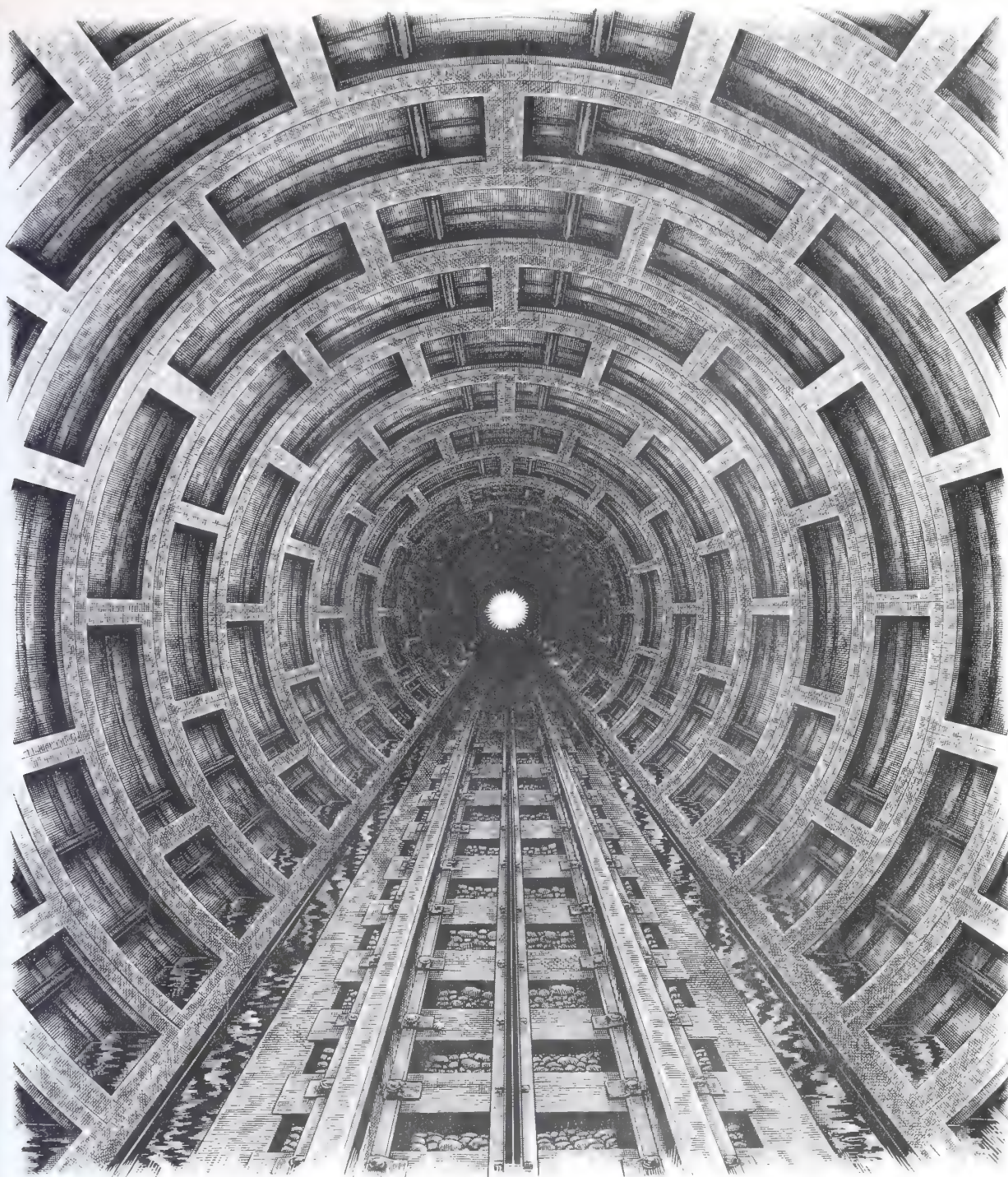
Eastern officials hope to head off Wallace off at the pass. "Another delay will accomplish nothing," says Eastern spokesman Robin D. Dole. For months, Eastern has been lobbying hard and trying to doubt Wallace's credibility. It also hopes that the new Transportation Secretary, Samuel K. Skinner, will listen to his predecessor, James Burnham IV, who criticized Eastern's union while in office and has since joined Eastern's law firm. Senator Bob Dole (R-Kan.), whose wife, Elizabeth, is Labor Secretary, called Wallace in for talks in mid-January, a source present at the meeting confirms.

PRESSURE. The unions are trying to persuade Washington, too. The House have been talking to Senator Alfonse M. D'Amato (R-N.Y.), who represents commuters who would be hurt by a strike. And at a recent meeting in Bal Harbour, Fla., the AFL-CIO's executive council called for an emergency board.

If Lorenzo persuades the White House to allow a showdown, the IAM will face tough going. Eastern hopes to persuade its pilots to cross an IAM picket line. And union leaders fear that up to half might do so. Eastern could then sign a deal with those pilots and sell off the balance of the carrier. To stop Lorenzo, the IAM hopes to escalate the conflict and spark a consumer boycott of Continental, hardly a sure thing despite the AFL-CIO organizing help.

But first Lorenzo must keep his Eastern dispute away from Congress, where his tough-guy tactics don't kindle much sympathy. If he can, he might just break the IAM. But then Eastern will be a shadow of its old self.

By Aaron Bernstein in Bal Harbour, Fla., with Pete Engardio in Miami, Stephen Payne in Washington, and Todd Vogel in Houston



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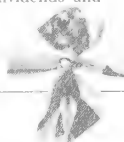
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BAD DAY AT WINDOW ROCK

If Navajo leader Peter MacDonald doesn't go, new business may

Throughout the Navajo Nation, Chairman Peter MacDonald is known as "MacDollar," in recognition of his free-spending ways. He paid hundreds of thousands of dollars to redecorate his suite of offices at the tribe's Window Rock (Ariz.) headquarters and chartered a plane to attend the 1988 Orange Bowl in Miami. In contrast to his predecessor, Peterson Zah, who dressed in Levi's and drove a battered

car from Tribal District Judge Harry Brown, who's married to a sister of MacDonald's wife. Meanwhile, council members are arguing over whether to appoint Vice-Chairman Johnny R. Thompson to head the 200,000-member tribe or elect a new chairman. MacDonald couldn't be reached for comment.

More than MacDonald's job is at risk. The turmoil threatens the tribal leader's economic development program, which

in capital, how to negotiate contracts for the tribe's natural resources, how to demand jobs and joint ventures as part of a deal. Unlike most tribes, which depend on a largely ineffective Bureau of Indian Affairs to negotiate for them, the Navajo have won business on their own by offering low-cost, productive labor, incentives, and sites near rail lines and interstate highways.

BITTER SPLIT. The Navajo narrowly elected MacDonald in late 1986 on his promise to bring jobs to the reservation where unemployment is 40%. He delivered: In 1987 he showed off the reservation at a high-powered economic summit. Since then, some 2,000 construction jobs and 800 full-time jobs have been created in industries as diverse as computer software development and mushroom farming. In June, General Dynamics Corp., which has operated an electronics assembly plant on the reservation since 1967, will open a second facility, employing up to 200.

MacDonald has brought hope to many young Indians, but his conduct has bitterly split the reservation and scared off prospective Anglo employers. Zah and others have talked of recalling the chairman for more than a year, though that is nearly impossible under the tribe's constitution.

The chairman's troubles began in July, 1987, when the tribe purchased Big Boquillas Ranch near Grand Canyon for \$33.4 million from Tracy Oil & Gas Co., which paid just \$26.2 million for it earlier that day. In the Senate hearing, the broker, a friend of MacDonald, claimed the chairman pocketed part of the profits. In addition, contractors say they paid kickbacks to MacDonald at the cost of doing business on the reservation. A federal grand jury in Arizona is looking into the charges.

The probe doesn't augur well for the chairman, but nobody is counting him out. He has risen from the ashes before. MacDonald, who once studied to be a medicine man and served in the South Pacific in World War II, served three four-year terms as tribal chairman before being ousted by reformer Zah in 1982. Four years later, MacDonald was indicted for taking bribes and his attorney F. Lee Bailey to defend him. Judge dismissed the charges after a trial ended in a hung jury.

This time around, the charges are more serious—and more is at stake. The chaos at Window Rock continues; the real losers will be the members of the Navajo Nation, who trusted MacDonald to bring desperately needed jobs to their remote land.

By Sandra Atchison in Denver



MACDONALD IS ACCUSED OF SQUANDERING TRIBAL FUNDS AND TAKING KICKBACKS

pickup, MacDonald wears pin-stripe suits and is chauffeured about the 24,000-square-mile reservation in a tribe-owned car.

Zah and other opponents have long accused MacDonald of squandering Navajo funds. But it appears now that not all that money came from the tribe. In Senate hearings in February, witnesses, including MacDonald's own son and an associate who taped conversations with the chairman, accused him of taking hundreds of thousands of dollars in cash, a leased BMW, and even a hot tub from non-Indians, or "Anglos," who do business with the Navajo. On Feb. 17 the 88-member Navajo Tribal Council put MacDonald on paid leave.

He's fighting the move. On Feb. 21, MacDonald's lawyer obtained a temporary restraining order against the coun-

cil has brought in Anglo companies after years of Navajo hostility toward outside employers. Other tribes could be affected, too, since they look for inspiration to the Navajo, the largest and richest American Indian tribe. With MacDonald gone, Indians would lose a powerful bridge to the alien world of capitalism.

MacDonald is a rarity among Indians in that he's fluent in the language of business. He understands how to bring

Since 1987 the chairman has brought nearly 3,000 jobs to the reservation, where unemployment is 40%

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EDITED BY HARRIS COLLINGWOOD

HOW IBM BROKE UP A HAPPY MARRIAGE

► Partly by working together, Compaq Computer and BusinessLand became billion-dollar enterprises. So what made Compaq suddenly decide to stop selling through BusinessLand in April? Simple. IBM.

Almost two years after launching its PS/2 line of personal computers, Big Blue is going all out to make the PS/2's so-called microchannel architecture an industry standard. IBM has enlisted BusinessLand to help it ensure the microchannel's success against a competing Compaq-backed architecture.

For months, IBM has pushed microchannel machines by offering fat incentives to BusinessLand and other chains. In return, IBM has demanded allegiance to the microchannel standard. The approach has worked. Industry sources say the retailer has raised sales commissions on IBM wares and cut them for selling Compaq gear. As a result, a profitable association has come to a bitter end.

A JUMBO ORDER FOR BOEING

► Boeing landed its biggest sale ever when Japan's All Nippon Airways ordered 20 747-400 jumbo jets for \$3.2 billion. In addition, ANA placed a preliminary order for up to 20 767-300 aircraft worth an additional \$1.5 billion. Boeing now has a backlog of 1,100 planes worth \$54 billion. ANA, Japan's largest airline and the eighth-largest in the world, will use the new aircraft to expand its international service.

POLAROID AND SHAMROCK TUSSLE

► Polaroid began a \$50-a-share, \$800 million tender offer for 22% of its stock—the latest defense in its battle

with raider Shamrock Holdings. But Shamrock, the investment vehicle of Roy Disney, has announced a proxy fight for control of Polaroid's board. Now it's going public with its plans for the instant photography company. Shamrock President Stanley Gold says he expects to sell some of Polaroid's undeveloped real estate, and he talks of licensing its camera technology to other manufacturers.

Polaroid has other ideas. In papers supporting the tender, Polaroid said it would introduce a "new generation" of instant film next year and a new consumer camera line in 1991. It estimated its 1990 operating profits would be twice those of 1988.

THE FCC PULLS A LICENSE

► The Federal Communications Commission needed just 10 minutes to decide to revoke the only AM radio license in Fredonia, N.Y. The commissioners found that Henry Serafin, the sole owner of Catocin Broadcasting, violated at least three FCC rules.

Serafin, they said, was guilty of racial discrimination when he refused to hire a black secretary. He even complained to the government agency that sent him a black applicant. Serafin also made false statements to the FCC

DROP THAT CATFISH, YOU VARMIN'T

Predators run rampant on Wall Street, but for sheer ugliness and rapacity, few can rival the double-crested cormorant, a hook-beaked bird that has become the scourge of Mississippi's burgeoning catfish industry. Now that catfish are a certifiably trendy food, Delta farmers are tending a sprawling, 90,000-acre patchwork of ponds. And the cormorants, known locally as

"water turkeys," have decided to do lunch. They now visit catfish country, migrating down from the Great Lakes, numbering roughly 100,000, the water turkeys each poach up pounds of fish daily, costing farmers about \$7 million a

Federal law permits farmers to kill just a few of the so instead they're shooting off propane cannons, fire and shotguns in a vain attempt to shoo the birds away are even buzzing their ponds with helicopters, with no success. If only those birds took greenmail.



about report filings. And he offered listeners a stereo receiver and cassette unit as a contest prize but kept it himself to use in the station. The last such revocation by the FCC was in 1984.

SPACEHAB WANTS TO SELL SPACE IN SPACE

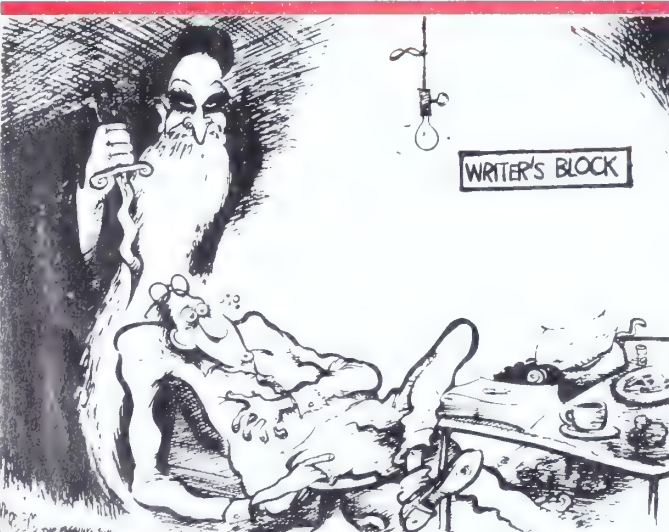
► Spacehab, a Washington-based startup, is aiming for the big time in orbit. The privately held company, headed by former NASA Administrator James Beggs, has asked Bear Stearns and Citibank to raise \$100 million to finance a

1,000-cubic-foot module for the space shuttle's cargo bay.

The module will allow researchers to work in spacesuits. Spacehab plans to market it through 3M, Aeritalia, Japan's Mitsubishi, and the European International consortium. No firm orders yet, but Spacehab has a ready reserved room on shuttle missions, with the first scheduled for 1991. The company will charge \$65 million a flight, of which \$28 million goes to NASA.

A POSNER GIFT TO THE HOMELESS

► Is Miami Beach firefighter Victor Posner one of the "thousand points of light"? One of the legion of volunteer-controlled companies, Crown Cola, has started a campaign featuring home Americans. Through American Red Cross and its bottlers will sell 6¢ for every 12 ounces of soda sold in 14 cities. The proceeds will go to local charities in each of those areas, which will count for 30% of the market. The campaign is related to a court settlement last year in which Crown agreed to pay \$3 million to a homeless program in exchange for a tax exemption.



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S LABOR AND DOLE WARM UP, BUSINESS IS FEELING A CHILL

To hear the chieftains of organized labor talk at their annual winter meeting in Florida, you'd think babies were their only business. With a fervor once reserved for organizing battles, the AFL-CIO is pushing federal legislation on child care, family leave, and a higher minimum wage for low-income families.

The emphasis on family issues is labor's bid to regain the influence it lost with the decline of union membership and organizing clout. "We want to be defined in a new way," says Gerald W. McEntee, president of the American Federation of State, County, & Municipal Employees. "It's good to show that we don't have a narrow view but are looking at a broader social agenda."

Since Democratic leaders and the Bush Administration are both interested in family issues, business could be the big loser. Labor has its best chance in years of moving its wish list. Its influence has been rising in Washington lately: Unions played a big role in shaping the 1988 Trade Act and were the driving force behind last year's anti-closing law. What's more, labor enhanced its standing within the Democratic Party when its members on the Democratic National Committee secured Ronald H. Brown's election as national chairman.

IN DOOR. And the AFL-CIO's agenda meshes with the plans of the Democratic leadership. Emboldened by the President's campaign pledges on child care, parental leave, and the minimum wage, Democrats have made the family a priority. Republicans are making overtures, too. On Feb. 21, Elizabeth H. Dole met with the AFL-CIO executive council in her first official act as Labor Secretary. "A considerable atmosphere of openness has been initiated," says AFL-CIO President Lane Kirkland, who called Dole "a personal friend."

That sounds like typical new-Administration honeymoon. But on at least one substantive issue—the minimum wage—the Administration, Democrats, and labor are moving toward compromise. Bush has given the nod to raising the

\$3.35-an-hour minimum, provided companies are allowed to hire new workers at a reduced "training wage." After years of adamant opposition to such a two-tier system, union lobbyists and Senate Labor & Human Resources Committee Chairman Edward M. Kennedy (D-Mass.) are reportedly drawing up a proposal that would allow employers to pay first-time workers less than the minimum wage for 30 days.

NASTY SITUATION. It's not clear whether the Administration will buy such a limited training wage. Dole says she will offer her own proposal in March. And other key issues offer less opportunity to deal. Dole says the Administration won't support a measure that requires employers to give workers unpaid leave to care for newborns and sick relatives. Instead, the Labor Secretary says she'll offer a plan to "encourage" employers to provide leave. Nor does Dole support a Democratic child care plan setting federal standards for day care centers.

These issues, plus the increasingly nasty labor-management situation at Texas Air Corp. (page 26), could bring an abrupt chill to AFL-Administration relations. But for now, business is worried. Industry lobbyists are vociferously opposed to parental-leave legislation, a proposal to require employers to provide health insurance, and an increase in the minimum wage. One business association representative bemoans Dole's selection of officials with little labor-management experience to staff her department. Although none of Dole's subordinates have been nominated formally, she has selected an assortment of aides who worked for her at the Transportation Dept. and Senate staffers who worked for her husband, Minority Leader Robert J. Dole (R-Kan.).

Without experienced aides around her, business lobbyists worry that Dole may be won over by labor's social-justice arguments while giving short shrift to businesses' concerns about the cost. Labor wouldn't mind that one bit.

By Susan Garland in Bal Harbour, Fla.



KIRKLAND: DOLE'S PAL

CAPITAL WRAPUP

AIR SAFETY

Airlines' pocketbooks will be hit hard when a special industry task force recommends new maintenance requirements for aging airplanes in late February. The panel will call for extensive replacement—rather than repair—of rivets and skin sections on Boeing Co.'s 727, 737, and 747 aircraft. The Federal Aviation Administration is expected to make the proposed rules mandatory. The work could cost an estimated \$50 million. And recommendations for work on other manufacturers' planes will follow over the next month or so. The proposals are the work of a group of airline and air-frame industry

representatives and safety experts that was set up after a recent spate of structural failures on aircraft.

THE JUDICIARY

Top officials at the White House and Justice Dept. are working to head off a mass exodus of federal judges and speed appointments to the bench. Justice officials fear that low morale caused by increasing workloads—and Congress' decision to kill a pay raise—will lead many judges to hang up their robes. The Administrative Office of the U.S. Courts says 42 judgeships are currently vacant. The office also says 10 federal courts are seriously strained because of multiple vacancies.

INVESTIGATIONS

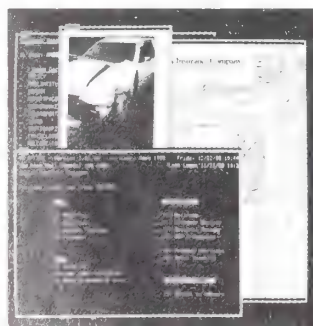
Pfizer Inc. may be the next company to feel the wrath of House Energy & Commerce Committee Chairman John D. Dingell (D-Mich.). He plans hearings to grill Pfizer officials on why they did not more quickly remove from the market an artificial heart valve, made by Pfizer's Shiley Inc. subsidiary. The valve has been implicated in the deaths of 160 recipients. The company says it acted responsibly. An aide says Dingell plans to make an example of Pfizer, showing how drug companies "victimize" consumers by marketing unsafe products and then lobbying against stiffer regulation.



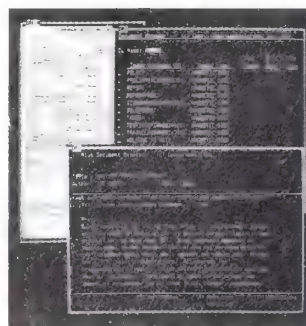
A BETTER IMAGE CAN DO WONDERS FOR CUSTOMER SERVICE. AND THAT'S NO IDLE CLAIM



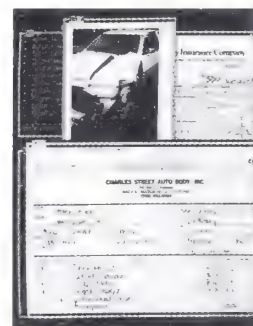
There's a fender bender on a freeway. The adjuster comes out and takes a picture of the damage. And signs off on an adjustment.



The handwritten document and the photo—the images—both go back to the home office via electronic mail.

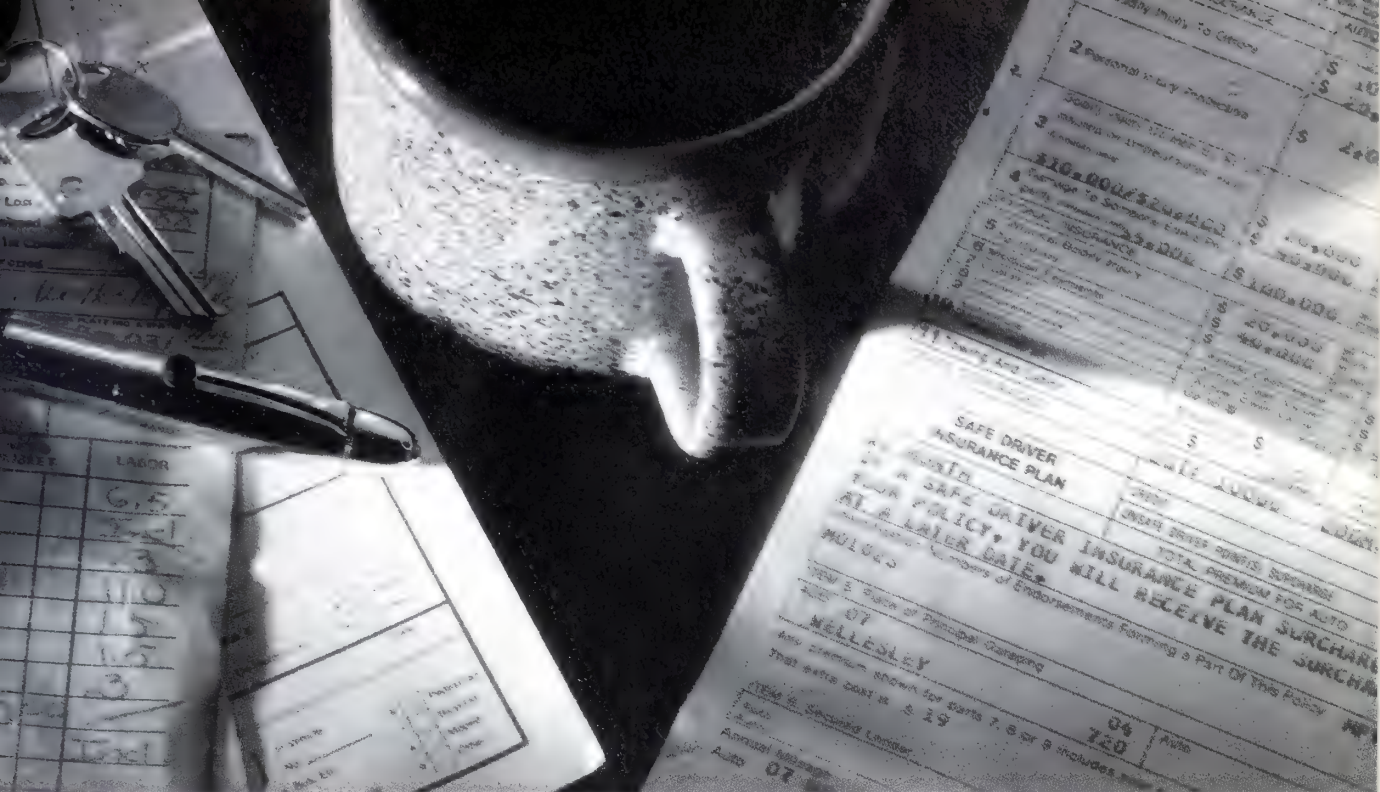


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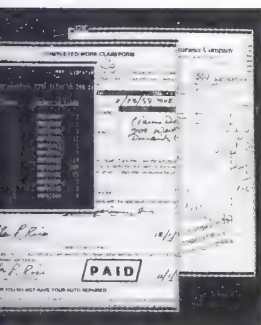
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BIG BANG: BIG BUST, BIG LESSONS

Rosy predictions give way to retrenchment as the City's major players lick their \$2 billion wounds

On the north bank of the Thames in the City of London sits Billingsgate, a historic 19th century fish market-turned-white elephant. The hulking brick building, into which Citicorp has poured millions of dollars, by now was to have been reborn as a model trading center where stocks, bonds, and foreign currency from the ends of the earth would change hands in high-tech splendor. But with its global securities business losing as much as \$200 million last year—a quarter of that in London—Citicorp is staying put in more modest digs while trying to rid itself of the lease on the unfinished building.

Citicorp's decision to bite the bullet comes at a time when securities houses throughout the City are still planning moves into new high-cost trading palaces designed in the days when bold global expansion was a given. Those days are over. Securities underwriting and trading volumes are still slumping in the wake of the 1987 crash (chart), and many experts expect the pressure on profits to continue. The City's major players have lost a staggering \$2 billion since Britain's ballyhooed Big Bang of 1986, when brokerage commissions were deregulated and banks and securities houses from around the world were allowed to compete freely against each other. Rather than paving the road to prosperity, however, the fallout is forcing firms to consider shifting some of their activities outside Britain. To many, Big Bang has been a Big Bust.

ATTACK. For now, London's preeminence among Europe's financial markets remains intact. And some players, namely U.S. investment banks, will surpass their prereach employment figures this year. London simply has too much in its favor: time zone, language, and a well-developed history and infrastructure of international trading.

Even so, it's clear that big chunks of business will come under attack from newly liberalizing bourses on the Continent. Foreign banks and brokerages have snapped up eight securities firms in Paris, where officials are aggressively

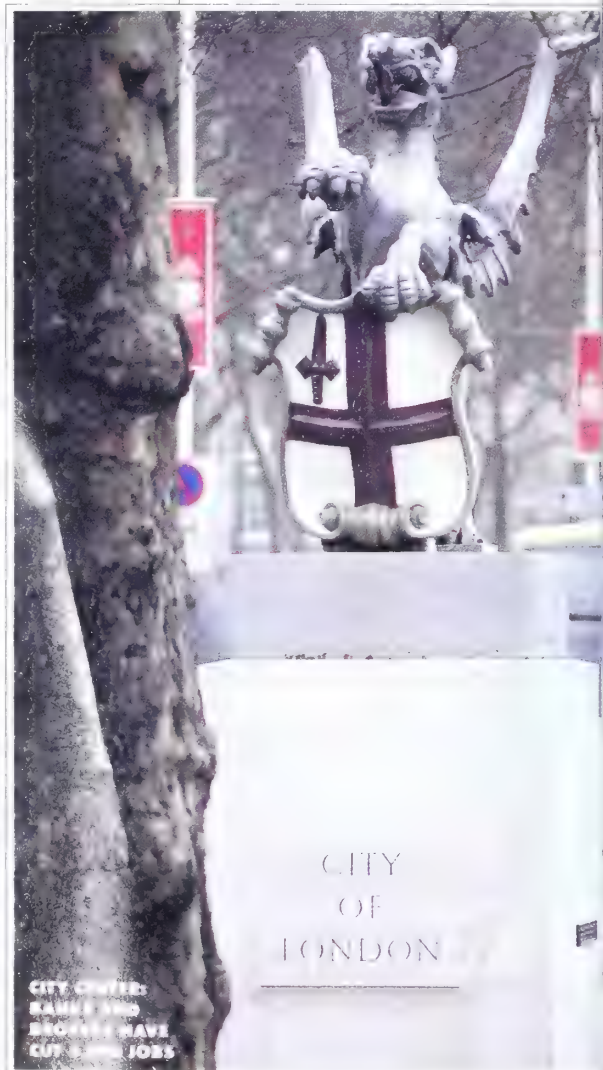
seeking to rival London. Britain's unwillingness to join the 10-year-old European Monetary System despite the 1992 deadline for scrapping European trade barriers also could hit the City. If a common European currency is introduced, Paris will seek to usurp London as a money-trading center.

The City's retrenchment is an embarrassment for Prime Minister Margaret Thatcher. Big Bang was partly designed to help make domestic players more competitive against international securities houses and to make London the most open market in the world. But the foreign banks, by and large, have made a shambles of the British brokers and traders that they acquired. And while Thatcher envisioned a thriving City creating thousands of new jobs, banks and brokers since the crash have eliminated a net 5,000 jobs—4% of the City's work force. As the City hunkers down for survival, "another 10,000 have to leave," insists Christian de Juniac, a director of Boston Consulting Group, which helped restructure Citicorp.

The most painful adjustment has fallen on the big American, British, and Swiss commercial banks, which jumped headlong into the ultracompetitive British securities business. For the most part, U.S. and Japanese investment banks have kept their powder dry, were solidly profitable in 1988, and are gradually building their Euro-

pean equity and advisory businesses.

Not so the banks. They typically paid premium prices for old-line London brokers only to discover enormous management, technology, and back-office problems. Chase Manhattan Bank pulled the plug on its equity operation in January, taking a \$40 million write-off. The new was worse from Union Bank of Switzerland in mid-February: Its Phillips Drew brokerage rang up losses of \$20 million over the past 21 months. And, c



21, National Westminster Bank PLC reported that its investment-banking lost \$98 million in 1988. A good sign of that came from the bank's decline in former corporate finance clients. Blue Arrow PLC, whose share price tumbled.

DOWN APART: Some of the more ruthless trimming has occurred at two big U.S. banks: Citicorp and Security Pacific Corp. By the end of this year, the work force at Citicorp's Scrimgeour Vickers subsidiary will be cut in half, to 350, from a year-ago level, as costs are also pared. And Security Pacific is signaling its hard-pressed British securities unit, Hoare Govett Securities Ltd., may be sold within 18 months if it can't be made solidly profitable.

To cut costs, Security Pacific has already shut departments that traded Eurombonds and British government securities, or "gilts." Says Peter S. Voss, CEO of Security Pacific Hoare Govett (Holdings) in London: "The idea that you need to become a fully integrated investment bank in lots of places around the world has been blown apart."

But out of such retrenchments a more ef-

ficient City eventually should emerge. But it will be a far cry from the politicians' and bankers' grandiose visions of the early 1980s. Many overseas bankers now admit that they couldn't crack the hold on the British securities markets maintained by such local powerhouses as S. G. Warburg & Co. and Barelays de Zoete Wedd. And most also concede that the volume of overseas stocks and bonds passing through London never came close to their rosy projections.

To survive in leaner times, Citicorp is regrouping around its core British securities business, into which it has pumped some \$300 million. It has sharply pared its coverage of stocks, dropped out of the gilts market, and, after discovering that it lost money on an astonishing 72% of the institutions it served, is dropping many of them.

The aim: make Scrimgeour Vickers one of Britain's top three brokers within three years. Says Peter H. R. Schuring, Citicorp's hard-nosed European investment-banking chief: "The initial concept of building a global equity operation was too ambitious to tackle all at once."

For most banks, there's another message: Such traditional strongholds as foreign exchange, swaps, and syndicated loans will provide most of the future growth, not stocks and bonds. For investment banks, though, almost everyone is zeroing in on mergers and acquisitions, figuring that Europe's takeover boom will inevitably gain momentum after 1992. Says Jeffrey Bowman, a vice-president of Standard & Poor's Corp.: "Merchant banking and investment banking are going to be the driving forces."

Led by Goldman, Sachs & Co., such U.S. houses as Morgan Stanley, Shearson Lehman Hutton, and First Boston are capturing the lion's share of the booming European merger business. In some cases they show up on both sides of a deal. In Italy's \$7.8 billion chemical merger last year, Goldman represented Enichem and Morgan Stanley advised Montedison.

Bolstered by such successes, several U.S. firms are going against the City grain by expanding their payrolls, mainly in investment banking. Salomon's London corporate-finance staff has doubled from a year ago, to 112 members, and is scheduled to expand by a third this year. "We clearly look at Europe and 1992 as a tremendous opportunity,"

says James L. Massey, CEO of Salomon Brothers International.

But the Yanks overseas still face substantial resistance from local players, including Warburg and West Germany's Deutsche Bank, which aren't expected to surrender European business to the City's upstart American merger makers.

"The old rules are being rediscovered," says John G. Heimann, CEO of Merrill Lynch Europe Ltd. "You cannot attempt to beat out the indigenous players."

If competition is heating up in investment banking, it remains cut-throat in securities underwriting and trading. Rebuilding around big investors and focusing equity research on a few industries with international companies, as most of the big players are, promises to be a slow process. Arthur Andersen & Co. estimates that European

stock-trading volume will grow at a languid annual rate of 10% to 15% into the 1990s—less than half its precrash pace. And big Japanese institutions, which captured a commanding share of the Eurobond market through bloody waves of price-cutting, are signaling that they now may have loftier ambitions. In January the giant Industrial Bank of Japan acquired a London Stock Exchange seat. Others are eyeing a more active role, too. Says John Howland Jackson, managing director of Nomura International Ltd. in London: "Our strength in Japan gives us breathing space to expand."

DEALER DEFECTIONS. Bond traders, who have been whipsawed by wildly gyrating interest rates, have lost \$330 million on gilt trades since Big Bang. What's more, domestic bond-trading volume has been contracting rapidly as the Thatcher government uses its budget surplus to buy back debt. The list of primary dealers has declined to 22 from 27 since deregulation, and some experts think that number could halve within a few years.

Although no one thinks in terms of the City's demise, its tough slog is far from over. Jacques P. Gelardin, chairman of Shearson Lehman Hutton International, took the ax to his London brokerage 18 months ago and has shaken up his management to get "comfortably in the black," he says. Even so, summing up the view of many, he adds: "We're looking at tough times for the next two or three years."

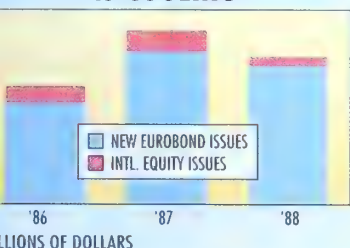
By Richard A. Melcher in London, with William Glasgall in New York and Blanca Riemer in Paris



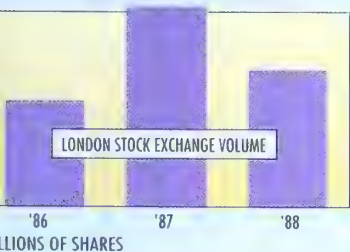
CITICORP'S SCHURING: "THE INITIAL CONCEPT... WAS TOO AMBITIOUS"

WHAT'S AILING THE CITY

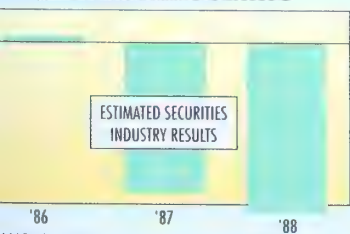
THE EUROMARKET IS COOLING...



...STOCK TRADING IS SLUMPING...



...AND LOSSES ARE MUSHROOMING



DATA: IDD INFORMATION SERVICES INC., BW



This Panasonic 27-inch color TV, complete with "Early American" style wood cabinet, now finding a home in Japan.

low TV sets from the U.S.A. are now making it in Japan.

began last June. A shipment of Panasonic 27-inch color TV sets—not imported from Japan—but exported to Japan. It was a bold signal that the Japanese market is ready to buy more products from the U.S.A. A signal sent by Matsushita (pronounced Mot-SOOSH), one of the world's largest electronics companies. But Matsushita is doing more than importing products from the U.S.A. It is also helping American companies that manufacture everything from computers to cosmetics to sell their products in Japan.

The Governor of Illinois said, "At a time when we hear so much about the balance of trade between Japan and the United States, it is encouraging to see American workers producing a product for export to the Japanese consumer market."

Another speaker said it differently, "We're loading them here and shipping them there."

FROM ILLINOIS TO JAPAN

When we were speaking about 5,000 TV sets from the U.S.A. headed for the Japanese home market. The 27-inch sets from Matsushita Industrial Company in Franklin Park, Illinois, are not only assembled in the U.S.A. but 70% of their components, including the picture tubes, are American-made products. Equally important, the product was designed in the U.S. specifically for

the Japanese market. To date, sales of the handsome wood cabinet sets in Japan have been encouraging.

Matsushita's involvement in strengthening U.S.-Japanese ties is part of a long company tradition that includes everything from establishing plants in Illinois, Georgia, Tennessee and other states, to funding professorships at MIT, Harvard and Stanford.

HOW AMAC CAN HELP SELL YOUR PRODUCT IN JAPAN

Indeed, Matsushita has formed a company—AMAC—whose major purpose is to help sell U.S. products in Japan. AMAC can help your company redesign a product to fit Japanese needs, arrange export licenses, set up introductions to key people, even help sell your product in Japan.

This recognition of international trade as a two-way street is part of a larger corporate philosophy—a philosophy that emphasizes "Human Electronics."

HUMAN ELECTRONICS

Matsushita Electric is devoting its research and development efforts to the concept of Human Electronics. Matsushita's objective is to develop and market products that make life richer, safer and more comfortable. In fact, we have developed over 14,000 products that are successfully fulfilling that goal. These products are sold worldwide under the brand names Panasonic, Technics, Quasar and National. In 1987, Matsushita's consolidated sales volume surpassed \$38.5 billion. All a direct result of a single-minded philosophy: Don't create new technology for technology's sake, but for man's sake.

MATSUSHITA ELECTRIC
PANASONIC TECHNICS QUASAR NATIONAL

MEXICO

SALINAS GOES AFTER ANOTHER MONSTER: THE PHONE SYSTEM

He wants to end the state monopoly—and tame the union



JOBS ON THE LINE: LABOR WANTS TO UPDATE THE PHONE NETWORK, BUT WITHOUT PRIVATE HELP

Just six weeks after jailing the leaders of Mexico's corrupt oil union, President Carlos Salinas de Gortari is taking on a second labor fiefdom: the Telephone Workers Union. The 36,000-member union is deep into negotiations with the state giant Teléfonos de México (TelMex) on wages, work rules, and, most important, Salinas' plans to privatize attractive sectors of the phone monopoly. He wants private investors to open as many as 60 new companies to offer cellular phone, facsimile, and other services. This is a key step in his plan to revamp Mexico's phone system and begin breathing new life into the economy.

Salinas comes to the talks strengthened by his victory over the oil workers. This time, though, he's likely to try concessions rather than strong-arm tactics to bring workers into line. He holds formidable legal weapons: If phone workers call a strike, he can force them back to work to protect national security. And army units are trained to run the system. But Salinas, widely viewed as anti-labor, sorely needs allies among workers to solidify political support and push through his plans to remake Mexico.

In a country where customers wait years to get a phone, Mexico's network needs a complete overhaul. TelMex will require billions in new investment for digital lines in four-fifths of the country.

Salinas' plan to upgrade the system would cost \$14 billion over the next five years, an unthinkable sum for a nation that has suffered a 50% decline in its living standard in this decade.

PACKAGE DEAL. Because of the huge investment, prospects are good that both sides will compromise and win loans from the World Bank and Japan. Foreign companies that sell equipment to Mexico, such as Sweden's L. M. Ericsson and France's Alcatel, are likely to benefit from the improvements, but the union sees Salinas' privatization plans as a step toward selling off the state's 51% stake in TelMex. It wants to prevent that most of all. While keeping his wage demands secret, Telephone Workers General Secretary Francisco Hernández Juárez says he has a plan to update the industry without private help. "We want to be part of President Salinas' modernization program," he says.

On the government side, officials deny that Salinas plans eventually to sell the state's share of TelMex. But many believe that's merely a negotiating tactic. To get the union to back private investment in the phone system, the government is likely to offer workers new training in high-technology equipment. Salinas seems intent on letting nonunionized phone businesses crack both the union's and TelMex' control. Ciudad Juárez

businessman Mario Aun, for example, is ready to start a \$12 million company to provide cellular service in north Mexico. It would be the first to break the state's monopoly.

Talks between the government and the phone workers are due to finish late March. If Salinas gets his way will mark a clear signal that he is on making private investment in Mexico's phone system attractive. Just as important, a peaceful outcome of the talks will show workers that Salinas has shrewdness to cater to their interests too. With important state elections coming up this summer, and Mexico's economic future at stake, the president will afford to put Mexico's workers permanently on hold.

By Stephen Baker in Mexico

SWEDEN

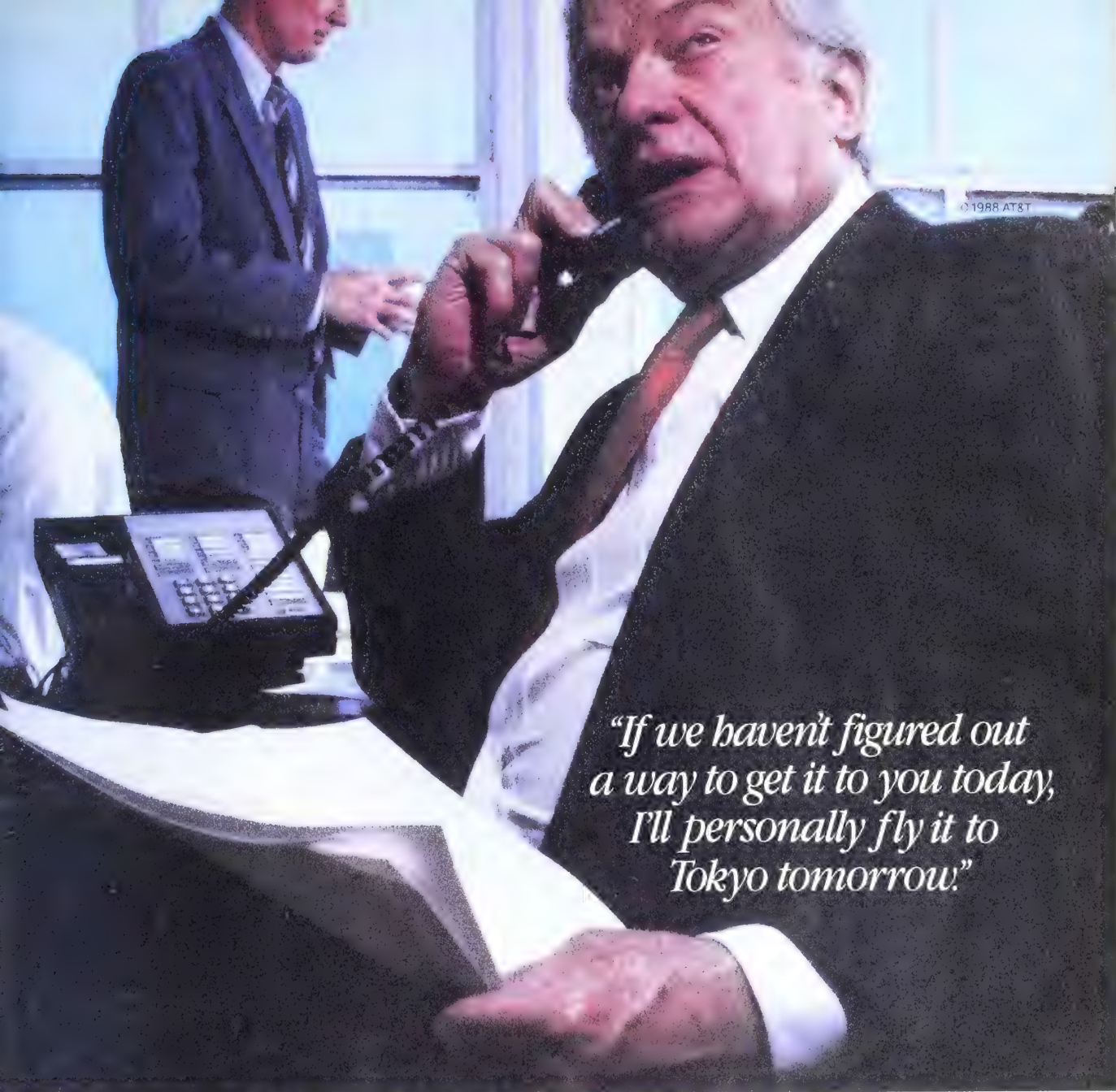
ERICSSON'S TRUE CALLING

It dumps computers to refocus switching gear and cellular phone

Weekday mornings at 6:30 a.m. when most Swedes would rather sleep an extra hour, Björn Svedberg works off the pressure of his job in savage tennis matches. The 51-year-old managing director of L. M. Ericsson, the stress has been high. His telecommunications company, nearly swamped by an ill-fated plunge into computers that slashed profits. Now, though, Svedberg is serving as The computer business has been dumped, 1988 profits were up 66%, \$307 million, and Ericsson's stock doubled, to 67, in one year.

No fancy tricks were involved. Svedberg simply refocused Ericsson on its core business: telephone switching and transmission equipment. And the move pushed Svedberg to find a buyer for his hemorrhaging computer business. "There was lots of criticism and tough discussions," he recalls. The computer business was sold to Finland's Nokia Corp. last year for \$217 million.

SLAYING GOLIATHS. At the same time Svedberg got a boost from skyrocketing demand for cellular phone service, which has turned his slow-growing equipment business into a hot performer. In just two years, cellular has doubled, to 10% of Ericsson's annual sales, which totaled \$5.1 billion last year. That growth should continue. Solid design and attractive financing has helped Ericsson capture 40% of the world market for cellular



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communications equipment. Svedberg solidified that position in January, when an Ericsson-backed design for digital mobile radio transmission was chosen as the U.S. standard by the Cellular Telecommunications Industry Assn. It had tough competition. Notes Ericsson Executive Vice-President Lars Ramqvist: "We went up against Motorola and AT&T, the two biggest boys in the business, and we won the standards war."

Until now, Ericsson's sales of cellular equipment have been mostly to private service operators. Those sales should net Ericsson 25% of the \$500 million U.S. equipment market this year. And with the industry's adoption of Ericsson's digital standard, the company has access to the far more lucrative Bell cellular market dominated by American Telephone & Telegraph Co. and Motorola Inc.

Svedberg could use more breaks as he

tries to outdo bigger rivals in switching and transmission equipment. After spending \$300 million on development, Ericsson's effort to sell switches to the Baby Bells in the U.S. has met with limited success. And AT&T just stole a huge deal from Ericsson in Italy. Even so, Svedberg insists things are looking up: "We've turned it around," he says. But he still needs his morning tennis.

By Jonathan Kapstein in Stockholm

HONG KONG

HONG KONG HOTELIERS START COLONIZING THE WEST

In the past year they've spent \$500 million on European and U.S. hotels

In Hong Kong, a guest arriving at the Peninsula Hotel enjoys such frills as a welcoming tea ceremony. Now, Hong Kong hoteliers, who have successfully transplanted that memorable level of service to Australia and elsewhere in Asia, are planning to bring it to the U.S. and Europe on a grand scale.

Over the last year, Hong Kong-based hotel companies have spent more than \$500 million to acquire hotels in North America and Europe. The names Regent, Peninsula, Mandarin Oriental, Regal, and Park Lane are turning up on the top luxury hotels in cities such as New York, San Francisco, Beverly Hills, and London.

ORIGINAL ART. The Hong Kong hoteliers are counting on service to provide their competitive edge. Labor, of course, is much more expensive than in Hong Kong, where the average hotel wage is \$2.50 an hour. So the companies cannot hire as many employees per room as they do in Asia. But with rigid in-house training, Mandarin Oriental, which manages a San Francisco property, has brought its highly personalized service to the point where it is already top-ranked after only 18 months of operation. And where the companies are building from the ground up or refurbishing, they are offering larger rooms and more grandiose bathrooms than other U.S. luxury hotels.

In January, Regent International Hotels announced that it will open a luxury hotel on Manhattan's East 57th Street in 1991. Its Japanese partner, EIE International, paid \$300 million for the prime site. Designed by I. M. Pei, the hotel will have oversize rooms with marble baths and walk-in closets. Rooms will rent for about \$400 per night. Just last August, Regent's rival, Hongkong & Shanghai Hotels Ltd., paid \$127 million—or more



SYDNEY'S REGENT: THE CHAIN IS PLANNING A NEW LUXURY HOTEL IN NEW YORK

than \$500,000 a room—for the former Gotham Hotel, on Fifth Avenue in New York. Now renamed the Peninsula, the hotel boasts oversize marble bathrooms, a health spa, and original artworks.

Both Hong Kong groups have targeted Beverly Hills, where the Regent on Feb. 11 held a \$100,000-a-head charity dinner to celebrate the reopening of the refurbished Beverly Wilshire Hotel. And Peninsula Group, Hongkong & Shanghai's marketing and hotel management arm, has agreed to manage a new luxury hotel, the Belvedere, being built in the same city by early 1990. Expected room rates: from \$240 to \$2,000 per night for a private villa.

Less famous but equally cash-rich, a second tier of Hong Kong hotel companies is emerging. Owned by Hong Kong Chinese families grown wealthy in real estate, these new players are using fi-

nancial muscle to crack the world market, aiming not only at five-star hotels but also at hotel management companies. Regal Hotels (Holdings) Ltd., controlled by entrepreneur Lo Yuk-sui, 49, recently bought control of the Constellation Hotel in Toronto for \$47 million. He then plunked down \$50 million for a 51% stake in Aircoa Companies Inc., of Denver, which manages 155 U.S. hotels.

YOUTH MOVEMENT. Park Lane Hotels International spent \$192 million last year to buy the Churchill Hotel in London from Kuwaiti owners, adding it to properties in Hawaii, Hong Kong, and San Francisco. It also has an agreement with Radisson Hotel Corp., of Minneapolis, to manage and franchise a chain of Radisson hotels in Asia. Last June, Y. Pao's World International (Holding) Ltd. paid \$135 million to buy Omni Hotels Group, a Hampton (N. H.) company managing 39 U.S. hotels.

Exporting top-quality hotel service is difficult. "You can't bring Hong Kong to the U.S.," concedes Regent's American founder and president, Robert Burr, who runs hotels in 12 cities and is building seven more. But Hong Kong hoteliers are trying. The Peninsula Group has a young staff at its New York hotel that is more enthusiastic than some of the more jaded personnel who have helped give New York a reputation for abruptness. The Regent is planning to assign a steward 24 hours a day to every floor of its 46-story New York hotel.

A major reason for Hong Kong's overseas expansion drive is keen competition at home. Tourism has grown by more than 20% a year for the past two years and hotel occupancy is around 90%. As a result, the hotels have raked in huge profits. But most see no room for further expansion in crowded Hong Kong.

The more ambitious of Hong Kong hoteliers would like to become as successful as Switzerland in exporting hotel expertise. Says Lo of Regent: "We aspire to become one of the leading hotel chains." If Lo and other Hong Kong hoteliers continue their big foreign push, travelers all over the world may be able to expect Hong Kong-style service wherever they go.

By Dori Jones Yang in Hong Kong



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The Sanwa Bank Limited New York Branch			

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WHY THE AYATOLLAH IS WHIPPING UP NEW WAVE OF FANATICISM

The Ayatollah Khomeini's death threat against author Salman Rushdie is recreating a belligerent political climate in Tehran that is reminiscent of the 1979-81 hostage crisis. When radical Iranian mullahs brewed their potent mix of xenophobia and Islamic fanaticism 10 years ago, their target was the American "Great Satan." Their goal was to seize the U.S. embassy and mobilize militant followers to wrest power from secular leaders such as former President Abolhassan Bani-Sadr.

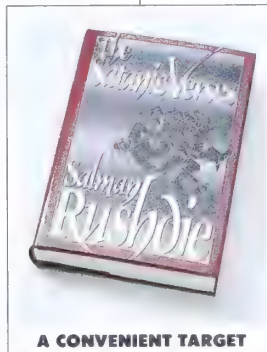
At this time the radicals aim to head off a push by pragmatists such as Speaker of Parliament Ali Akbar Rafsanjani to end Iran's isolation and rebuild its shattered economy by expanding ties with the industrial West. To overturn this effort, hardline clerics are stirring Moslem outrage against publication in the West of Rushdie's book, *Satanic Verses*, which they consider blasphemous. Khomeini, Iran's 88-year-old spiritual leader and political arbiter, called on Islamic zealots to kill Rushdie, a Moslem-born British citizen, and his publishers. It is a measure of Khomeini's power that his threat reverberated throughout Europe and the U.S., where Viking Penguin Inc. and booksellers would be targets. European Community members reacted on March 20 by ordering all 12 of their envoys home from Tehran for consultations—a warning that could lead to tougher reprisals if Khomeini's death threat were put into action. In the U.S., after several days of delay, President Bush also denounced Khomeini's threat.

LOSING CREDIBILITY. In the short run, the confrontation with the West will bolster the political position of Iran's radicals at home—but at an escalating economic cost. The resurgent hostility toward the West may delay or derail plans by Tehran's Minister and others to borrow badly needed funds for reconstruction. Talks on a \$2.7 billion German credit have stalled, and an official of the French Employers' Assn. says that political tension will "make it much harder to decide whether to open a permanent office or invest in Iran." So far,

projects such as Peugeot's \$1.8 billion, 10-year auto venture there appear likely to continue.

But the radicals are finding that politically, 1989 is very different from 1979. After their devastating eight-year war against Iraq, they have lost a lot of credibility. The free-market moderates have been gaining influence against the protectionist radicals, says Fahmy Howeid, an Egyptian writer and expert on Iran.

Outside Iran, too, the radicals seem to be losing clout. The fundamentalist revolution they hoped to trigger throughout Islam hasn't happened, although fundamentalism may gain ground in Afghanistan if Moslem guerrillas seize power following the Soviet pullout. But in Arab states, from the Persian Gulf to North Africa, moderate governments are trying to reduce tensions with the West over Rushdie's book, even though they have joined in condemning it. In Pakistan, right-wing religious parties stirred protests against the book to pressure Prime Minister Benazir Bhutto, a woman leader backed by a secular party in a Moslem country. But Bhutto has tried to down-



A CONVENIENT TARGET

play the issue.

Until recently, Khomeini had been using his influence within Iran to keep a political balance between radicals and pragmatists. He may have decided to whip up a new wave of fanaticism because he sensed that the fundamentalist tide has been ebbing in most of the Moslem world. By persisting with his death threats, Khomeini runs the risk of a serious blowup between Iran and the West. A cutoff of Western economic ties that are crucial to recovery would be a disaster for Iran. In the past, Khomeini has shown that he can reverse failed policies, as he did when he decided to end the Iran-Iraq war. But now he appears to be turning a deaf ear to the pragmatists' argument that what Iran desperately needs is peace and stability, not more revolutionary fervor.

By Susan Carter in Bahrain, John Rossant in Rome, Frank J. Comes in Paris, and John Templeman in Bonn, with bureau reports

DEAL WRAPUP

PHILIPPINES

Business is picking up in the Philippines, spurred by growing confidence in the country's political stability. A surge of construction in Manila, from office and apartment buildings to shopping malls, is the most visible sign of the revival. And U.S. companies are expanding their operations, although there are few new U.S. investments. After Corazon Aquino became President in 1986, business was dampened by coup attempts. But that threat appears to have faded. Now 20 of the 55 U.S. companies with major Philippine operations plan to invest \$600 million to expand over the next three years.

Coca-Cola Bottlers Philippines will put \$250 million into additional bottling plants, and Caltex Petroleum Corp. will spend \$105 million to upgrade refinery and distribution facilities. On the horizon are two big U.S.-led investments. Taiwan-based U.S. Industries Far East is a partner in a \$320 million petrochemical project. And California-based American Technology Group plans a \$65 million semiconductor operation.

CHILE

An expanding economy should smooth the transition to a democratic government next year after 15 years of rule by General Augusto Pinochet. Gross national product is likely to

grow by more than 5% this year after a record-breaking 6.8% in 1988.

Patricio Aylwin, a 70-year-old lawyer and leader of the Christian Democratic Party, Chile's biggest, is expected to win next December's presidential election as the opposition parties' sole candidate. Parties that backed Pinochet could pick Finance Minister Hernán Buchi, 40, a Columbia University-trained mathematician, as their candidate. Meanwhile, extreme-left groups, by keeping a low profile, appear to be avoiding provocations of the military. But Pinochet's announcement this month that he intends to stay on as army chief points to a potential source of future civilian-military tension.

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A KINDER, GENTLER BUSINESS CYCLE?

Why those big economic swings may be history

Experience teaches that all good things must come to an end. An economic recovery begins, growth rebounds, and the expansion is rolling. But just as surely as thunder follows lightning, contraction follows growth. Now economists, who watch every wiggle on the charts, think they detect the telltale signs of an expansion entering the danger zone. Producer prices jumped 1% in January. Employment surged by 200,000 jobs. So, if interest rates

rebound, Kudlow, chief economist of Bear, Stearns & Co., "the growth phase could last 10 years."

Except for the 106-month expansion fueled by Vietnam war spending in the late 1960s, no upturn since World War II has lived this long (chart). The economy typically works up to a boom in year three or four. As labor markets tighten and production capacity hits the ceiling, a wage-price spiral carries inflation upward. The next ominous sound is a

trick—successful so far—has been saving the economy just enough to maintain growth-choking squeeze unnecessary. "Credit gets scarce earlier," explains Roger E. Brinner, chief economist at Data Resources, "so it doesn't need to get as scarce." No crunch, no bust.

The worry now, of course, is that the Fed might carry restraint too far and topple the expansion. Those same fears surfaced in early 1984, when Fed governors moved to cool off a recovery that was thought was moving too briskly. The medicine didn't kill the patient then, but it shouldn't now.

■ **Balancing sectors.** Mostly thanks to good luck, different sectors of the economy have taken off at different times. Since 1982, the oil patch, manufacturing, the farm belt, and the financial services industry have all contracted in turn. But because no single sector accounts for that large a portion of the economy, and because many of these downturns

occurred in distinct geographic regions, the combined impact was not enough to drag the overall growth number down. "In effect, we have had a kind of stagflation," says John Win Kellner, chief economist at Manufacturing Hanover Trust Co.

■ **Capacity.** While some industries report slowing utilization rates, overall capacity, now at 84.4%, still has considerable leeway before it hits the previous decade's high of 86%. And the increases have come in industries that could handle them—such as autos, with 75% utilization rate—

have some slack. Others, operating comfortably in 1987, have utilization rates in the low 80s now but are adding capacity. All this means capacity is not so constrained that prices will surge, forcing the Fed to clamp down hard.

■ **Employment.** Labor resources seem to be abundant. The dreaded "employment" rate, or the flashpoint at which wage pressures nudge inflation upward, may be a lot lower than it is to be. For one thing, the composition of the work force has changed radically since 1980. The baby boomers who swelled it are nearing an age when they're likely to stay put—behavior that naturally tends to reduce the jobless rate. Second, although the population is growing at a slower rate than during

THIS IS ALREADY THE LONGEST PEACETIME EXPANSION



are a percentage point higher than they were in November. Will the expansion's seventh year be its last? Maybe. But a wealth of evidence says it doesn't have to be.

The economy today acts very differently from the way it did only a decade ago. Financial deregulation has changed the way markets behave, so interest rates move quickly in response to inflationary fears. Global competition has made the U.S. economy more open, so trade plays a bigger role in determining output. Service industries, long the predominant employer in the U.S., have grown still more important. The new conditions have all had the same effect on the business cycle: They work to flatten the swings in growth and make the upside of the cycle last longer. In the case of the current expansion, says Law-

crunch, when investors and the Federal Reserve Board respond by hiking interest rates. Demand gets choked off, output and employment fall, and the cycle heads back downward.

This time the familiar drama isn't playing out. Instead of accelerating to an unsustainable rate, growth has kept up a slow and steady pace. Here are some ways in which the economy is deviating from the classic boom-bust script:

■ **Fed policy.** For the first time in decades, the Fed has moved into retreat. Fed Chairman Alan Greenspan's gradual tightening in the past 10 months deserves credit for keeping the expansion on track—and the markets are applauding his actions. If this business cycle has had a hero, it may well have been the vigilant Fed. Its small, preemptive moves toward tighter money have calmed inflation fears. The



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the 1970s, more people are going to work. The labor participation rate has been rising steadily, from 64.1% in 1983 to 66.2% in 1988, as dual-income households proliferate.

■ **Inventories.** Traditionally, inventory mismanagement could plunge the economy into recession. But recently businesses have been doing a good job of keeping their stockpiles lean and mean. While factory inventories rose 0.7% in December, the inventory-sales ratio remains comfortable, with 1.5 months' worth of goods on hand for one month of sales. More recently, however, dealer lots have been crammed with unsold autos, and Detroit may be forced to go to incentives. That could help right the imbalance between stocks and sales.

■ **Trade.** The recovery began in November, 1982, with an unusual mix of fiscal stimulus and relatively high interest rates. Consumer spending surged, and the economy took off. The combination of strong output and high real returns attracted foreign investors to the dollar, and the currency started to climb. The strong dollar made imports cheap—a blessing early in the expansion, when domestic producers couldn't have met rocketing demand without severe bottlenecks. By the same token, the dollar's reversal since 1985 has boosted exports, giving U.S. manufacturing, and overall output, a much-needed lift.

Still, there are some who think classic end-of-cycle symptoms are already apparent. Prices are rising, bringing on the higher interest rates that make debtors vulnerable, says economist Allen Sinai of Boston Co. With balance sheets overextended, the inevitable will happen: Consumers will put their spending plans on hold, and manufacturers will cut back on shifts. The downward spiral will begin. Agrees Robert G. Dederick, economist at Northern Trust Co. in Chicago: "There's no reason to think we've mastered the art of the soft landing."

But attentive markets and a nimble Fed have certainly striven to do so. Today, "bond market vigilantes," hypersensitive to signs of inflation, force the Fed to tighten preemptively, says Edward Yardeni, chief economist at Prudential-Bache Securities Inc. And businesses have worked hard to manage inventories and plant capacity more deftly—responding, in part, to intense foreign competition. So there's no law that says the economy has to tumble into recession. The business cycle may not have been killed, but it has certainly been subdued. These days, asserts Brinner, the cycle swings between 5% and 1% GNP growth instead of 7% and minus 1%. If he's right, the good times may not end with a bang. And the bad times that follow may not be so bleak.

By Joan Warner in New York

Marketing

RETAILING

AIRPORT SHOPPING GETS AN UPGRADE TO FIRST CLASS

Better retailers are expected to generate more revenues

As millions of stranded air travelers can attest, U.S. airports are among the worst places in the world to eat and shop. Home to greasy "buffeteria" restaurants and tacky souvenir shops, airport concessions have earned a reputation for poor quality and sky-high prices. Says Tom Moriarity, senior associate of real estate consulting firm Halcyon Ltd. in Washington, D.C.: "In airport planning, retail was generally an afterthought."

But now, as airports seek to attract a more affluent audience. "Airport concessions have come to expect a certain level of retail service. Ten years ago it wasn't the case," says Susan M. [unclear], general manager of aviation, customs and public services for the Port Authority of New York & New Jersey.

Already, mainstream retailers are moving out to the airports. The Bloomingdale's department store chain left its New York City store in November, 1986, by opening Bloomie's Express clothing and gift



Now that attitude is changing. As dozens of domestic airports remodel terminals for the 21st century, they're giving retail space almost as much thought as runways and gates. Upgraded shopping areas are becoming an important airport marketing tool, a way to enhance images and generate greater revenues.

CAPTIVE AUDIENCE. Better stores are also a by-product of airline deregulation. Nearly 1 billion passengers a year pass through the nation's airports. Flight delays of more than an hour create a cap-

tive, affluent audience. "Airport concessions have come to expect a certain level of retail service. Ten years ago it wasn't the case," says Susan M. [unclear], general manager of aviation, customs and public services for the Port Authority of New York & New Jersey. Already, mainstream retailers are moving out to the airports. The Bloomingdale's department store chain left its New York City store in November, 1986, by opening Bloomie's Express clothing and gift

Even traditional airport conces-

, such as Marriott's Host International and Greyhound's Dobbs Houses, have been moving upscale. They're introducing outlets that focus on regional products, including an Ozark handicrafts store at the St. Louis airport and a Northwest Shop featuring Eskimo carvings and local wines in Seattle.

Such moves are just the beginning. As part of the Port Authority's \$3 billion "2000" redevelopment, which includes construction of a new central terminal complex, the agency has commissioned a \$250,000 study by Halcyon to determine the best mix of food and retail outlets for the airport. One idea: a cluster of "Best of New York" boutiques run by museums and prominent local retailers. "The airports have gone wrong in concentrating on \$40 T-shirts," says John R. Haden, director of marketing for Atlanta's Hartsfield International Airport, which may add 130,000 square feet of commercial space over its main terminal.

WINDFALL. It's not hard to see why airports would start landing at airports—but what took them so long? Airports have typically awarded space to the highest bidders, not necessarily the best operators. And airports aren't ideal retail environments. Shops must stay open a few hours to accommodate flight schedules, while security requirements make deliveries difficult. "The airport is not a windfall business," says Dickson, senior vice-president of Paradies Shops Inc., an Atlanta-based operator of 150 airport stores. "It's high investment on short-term leases."

Airports have been trying to lessen their risks. Instead of picking tenants based on who will pay the highest rents, they then get built into prices, many airports now consider a business plan that includes pricing, merchandise mix, store layout. "Better airports made an unconscious decision that they may get a rent in exchange for lower retail prices and better-quality facilities," says John L. Izant, vice-president of corporate development for Host International. When Host won a 10-year lease for an 800-square-foot open mall featuring art gallery and a seashell shop at Tampa International Airport, Izant says, "We did not have the highest bid, but we were very high on design and pricing." Lower prices mean more sales—on which airports make a percentage.

Airports will always have their limitations as retail centers, though. "You can't turn an airport into a shopping mall," says Dickson of Paradies. "The airport customer only has 35 minutes to stop and is looking for convenience and impulse items." Bloomie's Express and McDonald's may take wing, but a full-grown Sears will never fly.

By Amy Dunkin in New York, with Matt Ticer in Atlanta and bureau reports



HOW EUROPE 1992 COULD COST ITS AIRPORTS \$2 BILLION

Forty years ago a few enterprising Irishmen started selling tax-free whisky and cigarettes to transatlantic passengers whose planes stopped to refuel at Shannon Airport. Europe's duty-free sales have mushroomed to \$4.7 billion since then, largely on purchases made by travelers flying from one European country to another. But now that duty-free business is in jeopardy. The European Community's plans to apply a uniform value-added tax after 1992 will make duty-free shopping obsolete for travelers between the 12 EC countries. That could mean a loss of \$2 billion in sales.

Since European airline deregulation in 1986, the number of air travelers throughout Europe has grown by about 10% a year, to nearly 500 million. To accommodate bargain-hungry passengers, airports serving cities from Paris to Frankfurt have built sprawling duty-free malls that sell everything from alcohol to Danish furs and French designer shoes. With Europe's steep taxes on a wide range of products, a bottle of Johnnie Walker Scotch at London's Heathrow airport can go for less than one-third of its price in downtown Copenhagen. Hermès scarves and Yves Saint Laurent perfumes sell for about one-fourth less.

NEW APPEAL. Since duty-free is such a big business, it's no wonder that lobbyists are battling EC officials to keep it alive. A Brussels-based duty-free lobby projects that sales will drop at least 40% after 1992. Market leader Yves Saint Laurent Parfums estimates that 60% of its sales could be jeopardized.

The loss of duty-free business could hurt airports and passengers alike. Some airports get up to 20% of revenues from tax-free sales, and they may have to make up the difference in higher landing fees and ticket prices. "We can't think of anyone who doesn't benefit from duty-free shopping, so why do away with it?" says Barry Goddard, director of Britain's duty-free confederation. But one EC customs official calls it "unthinkable" to maintain a tax-free market in an economically integrated Europe.

To ward off the blow, airports are scrambling to broaden the appeal of their retail stores. Voltaire's Antiquités at Charles de Gaulle airport near Paris is known more for sparing clients the trouble of getting merchandise through customs than for the 10% value-added tax savings. At the Copenhagen airport, the growth is in non-duty-free boutiques selling Danish silverware and down comforters.

Tax changes may also shift the duty-free game outside EC borders. The Swiss are talking about charter flights from Majorca to London that would touch down in non-EC Geneva for a duty-free shopping spree. And the Swedes have big plans for international waters. By offering day cruises to not-so-distant, non-EC islands, Stena Line hopes to attract diehard duty-free shoppers who want to bypass EC regulations. After all, some people will go anywhere for a bargain.

By Bettina Baudoin and Frank J. Comes in Paris, Dana L. Hawkins in Brussels, and bureau reports

NATIONAL INTERGROUP: HOW PETE LOVE WENT WRONG

Let's diversify, the steelman said. And then the troubles began . . .

It was a vintage performance by Howard M. "Pete" Love, the tall, ambassadorial chairman of National Intergroup Inc. Last July, at the annual meeting in Pittsburgh's posh Vista International Hotel, Love spoke glowingly of the future of his diversified metals, oil, and drug company. Never mind the previous year's loss, he admonished investors. NII's fiscal first quarter, which ended in June, was profitable. The company was on its way back.

Just three months later, Love reported that NII would have to take an unexpected write-down, assuring a fourth straight year of losses. Investors were outraged, but not totally surprised. For the past five years, Love has promised that his strategy of moving the former National Steel Corp. into exciting, high-growth businesses was about to pay off.

This time, however, Love seems to have made one unfulfilled promise too many. NII's bankers withdrew, forcing Love to get new lenders for the second time in 12 months. Love has also begun to lose the unqualified support of his board. Former Westinghouse Electric Corp. Chairman Douglas D. Danforth, a relative newcomer, has been unflinching in his pressure for results. So, as many investors clamor for Love's ouster, he has relinquished much of his responsibility to President Laurence J. Farley, a former Black & Decker Corp. chief executive he recruited a year ago. "Most decisions are being made by Farley," says a company banker. "He was hired for a purpose: to help turn around NII."

National Intergroup's future looks about as shaky as Love's. The company has botched efforts

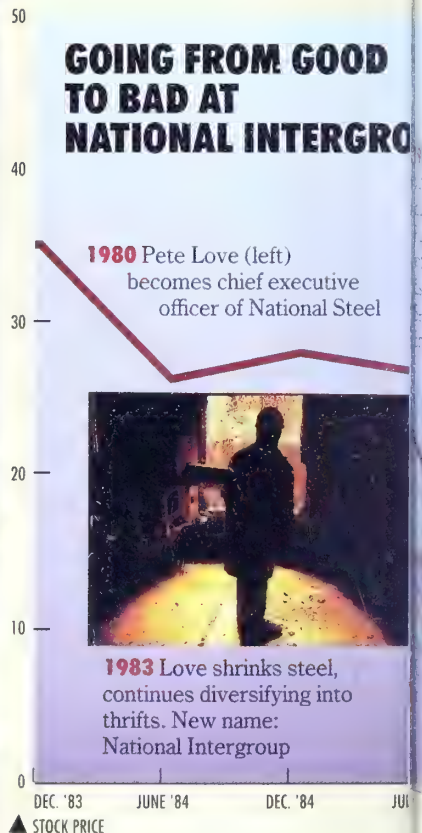
to get into oil and drug wholesaling, and its steel business is the least profitable of the big producers. No wonder Houston takeover artist Charles Hurwitz has been accumulating stock. "If Hurwitz makes a fully-financed cash offer," says one director, "we're up the creek."

Love and his directors may lose their jobs. But the real losers are NII's public shareholders. During Love's tenure, NII lost a total of \$535 million. As a result, while the market value of most major steel companies has risen dramatically since Love took over NII in 1980, his company has bucked the trend. It is worth a mere \$400 million today—about two-thirds as much as when Love became chief executive.

The tale of that decline involves an impressive cast: scions of old-line indus-

trial families, entrepreneurial dealmakers, and some of the nation's best-known leveraged buyout professionals. What's more, the moral illustrates a classic flaw of corporate control in America: As is the case at many corporations, NII's top officers and directors don't own much stock in the company. Does that matter? Students of management argue that directors who don't have much of a financial stake often fail to monitor management performance effectively. Moreover, many of NII's outside directors have longtime social business ties to Love and didn't rock the boat.

FISHING SAFARIS. One reason may be that Love was a CEO out of central casting. Born into an influential family, went to Exeter, Colgate, and Harva-



ess school. Just five years ago he the bright light of the steel industry. When foreign competition bore , he led the way among domestic acers by downsizing and making opns efficient. And he was hailed as onary for vowing to diversify.

what happened? For one thing, crit-ay Love relished the trappings of fice far too much. Described as an entee manager" by former col- es, Love spent a good deal of time outside boards and civic organiza-

He would take frequent trips— fishing in Iceland, for instance, people like Roger B. Smith, chair- of General Motors Corp. Love fan- himself a dealmaker, but his record s a pattern of paying top prices for esses that quickly developed big ems.

r his part, Love says his outside ties never distracted him from run- NII. Many of his trips were busi- related; GM's Smith, for example, is stomer as well as a friend. Love es aside NII's losses as partly the t of unfortunate timing: Oil prices st after he bought a crude-oil ship- and an industry price war broke out s he purchased a drug distributor. ne criticism, he says, comes from -term-oriented investors who don't stand that a wholesale diversifica- takes years to accomplish. Besides,

if he hadn't moved away from steel, NII would have gone bankrupt. Love argues that while his promise of big profits is behind schedule, NII will be flying by the mid-'90s. "Shareholders are better off by having a well-run, well-positioned drug company," he insists.

Perhaps. But Love made his biggest mistakes whenever he tried to diversify. He was a steelman to the core. His first job was measuring slab for \$700 a month. He spent his career climbing the ladder at National Steel, where his father, George, was vice-chairman. It was a hard act to follow: The legendary George Love helped create Consolidation Coal, headed iron ore giant M. A. Hanna, and was chairman of Chrysler, a National Steel customer.

SPREAD THIN. Aided by his contacts and earnest nature, young Pete rose briskly. At 36, he headed National's Midwest Steel Div. in Portage, Ind., and by 45 he was president. "Pete was brilliant, but he also was the favorite son. He was influential in sales because of his father's contacts," says R. T. Ernest, a former manager who worked with Love for 15 years at Midwest.

Just as Love became chief executive, National had acquired one of the nation's largest and best-managed thrifts, First Nationwide Financial Corp. Love wowed Wall Street by selling off a mill to workers and half of his steel unit to

Japan's Nippon Kokan. In 1984, when the U.S. steel industry lost billions, Love's restructuring brought in \$53 million in net income. "Pete was very impressive," recalls Elmer B. Staats, a former director and former U.S. Comptroller General.

Meanwhile, Love asked management consultant Bain & Co. to find other fields for NII. Bain suggested building on NII's expertise in wholesale steel distribution. But Love picked another option further afield: drug distribution. A deal appeared on Love's doorstep in the summer of 1984. Emil and Robert Martini, the brothers who ran Bergen Brunswick Corp., the nation's second-largest drug distributor, wanted to talk.

Bergen, based in Los Angeles, was growing rapidly by supplying drugs to pharmacies and hospitals. To Love, this was it—a business that wasn't cyclical, didn't need lots of high-priced labor, and was thriving. A number of investors howled, however, when he proposed selling NII in a stock transaction worth \$28 a share—nearly a 30% discount to NII's book value.

Love won approval in March, 1985, after a bitter shareholder battle, but a stunning announcement scuttled his merger. NII had to reduce its stellar 1984 results by 74%. Unbeknownst to Love, his aluminum managers had been speculating on metals prices for years, and had lost big. Wary of other hidden problems, the Martinis backed out.

Their instincts were on target. At a difficult time for NII, critics say Love was paying too little attention to operations. Instead, he was a director of more than a dozen other organizations, attending scores of board meetings annually from Monsanto Co. in St. Louis to Transworld Corp. in New York. And he was active on the Pittsburgh civic and social scene. This took a toll at NII. "You were lucky if Love stayed in a meeting for 20 minutes," says one alumnus. Love denies that, however, and says he has always worked 12-hour days, up to six days a week.

FAST MOVES. Stung by the aluminum loss, Love tried to reassert control. He took the steel unit from James E. Haas, who, as president and COO, oversaw NII's daily operations. But to managers' consternation, Love didn't cut back on his outside activities. "Pete still wasn't minding the store," says a former executive. "You can't turn around a company by being a social butterfly," he adds.

By the summer of 1985, NII attracted a takeover bid from Leucadia National Corp., a major investor that opposed the Bergen deal. Love leaped into action. He sold the thriving thrift business to Ford Motor Co. for \$426 million. Then he acquired Permian Corp., the nation's largest oil distribution company, from the

84 National
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1987 William Tauscher (below) says his Foxmeyer unit will make money. Love forecasts profits—but losses continue



1986 National piles up debt to buy drug wholesaler Foxmeyer. Losses widen as price war begins

85 Merger
al falls through.
tional sells thrifts,
ys oil shipper.
nds year with loss as
etal prices plunge

1988 A Foxmeyer write-down causes a loss at National. For the second time, Love's bankers defect

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PRESIDENT FARLEY NOW HAS THE REINS AT NII AS THE CLAMOR FOR LOVE'S OUSTER GROWS

leveraged-buyout firm Wesray Capital Corp. Its major partners were Raymond G. Chambers and William E. Simon, the former energy czar and Treasury Secretary who had made a fortune by buying cheap and selling high. Love seemed to get off lightly when he paid \$400 million, or four times cash flow, for Permian. But then oil prices fell, and Permian began to lose money.

Bain was lukewarm about Permian, and several directors expressed reservations. "Servicing stripper wells in Texas is not one of the all-time growth industries," says former director Anthony M. Frank, who is now U.S. Postmaster General. The NII board, however, ended up approving Love's deal unanimously. It did offer a plus: Wesray effectively shut out Leucadia by taking a 14% stake in NII and two board seats.

In the fall of 1985 another seller came calling. This time it was 35-year-old William Y. Tauscher, co-founder of Foxmeyer Corp., a fast-growing drug distributor with sales of \$1.2 billion. The son of a Caterpillar Inc. manager, Tauscher became an IBM salesman after graduating from Yale. He then latched onto some venture capital and started building Foxmeyer. He bought a rash of small distributors and linked them with his sophisticated accounting and warehouse system.

Tauscher was an aggressive dealmaker, straight out of *Bonfire of the Vanities*. Just before contacting Love, he had tried to arrange a leveraged buyout of Household International Inc.'s merchandise units for nearly \$700 million. When it fell through, Tauscher turned to National Intergroup. "He was as savvy at doing deals as most invest-

ment bankers," says a friend. But by the time he met Love, Tauscher saw that Foxmeyer's growth was peaking. The industry was consolidating, and a shake-out was on the way.

Love had Haas, his top steel distribution specialist, scout out Foxmeyer. An abrasive, tough negotiator, Haas tore into the disclosure documents. They predicted soaring profits. A quick study by Bain, however, raised red flags. Under Haas's microscope, Tauscher's projections "didn't hold up to the light of day," says a former NII executive.

FLIP CHARTS. After two testy meetings in New York with Tauscher and his investment banker, talks broke off. They began anew only after Tauscher persuaded Love to cut out Haas. Love says he can't recall any such wrangling, but

sources say Love led the talks from then on. Tauscher proved to be a good salesman. Scribbling on glossy flip charts, Tauscher forecast that operating profits would more than double in two years.

Tauscher created a horse race by shopping Foxmeyer to other parties, including Bergen Brunswig. NII's deal with Foxmeyer mysteriously leaked out in early 1986. Foxmeyer common rose to 30 from the low 20s, prompting an inquiry into Foxmeyer's stock activity by the Securities & Exchange Commission. Former Foxmeyer and NII officers were deposed, according to several sources, but the SEC never took any action. Tauscher says he had nothing to do with the leak.

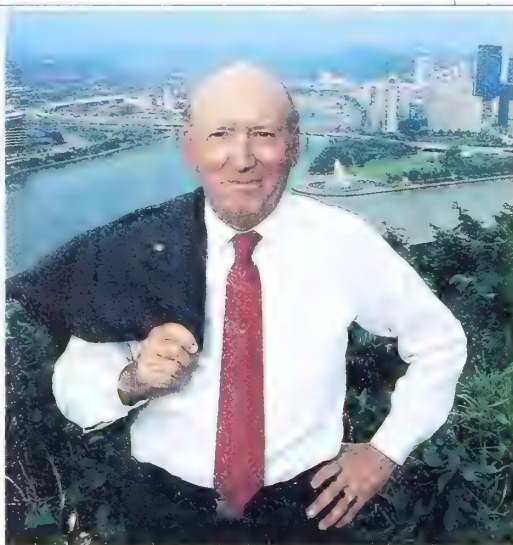
Foxmeyer's stock runup spurred Love to rush the deal. He proposed that NII buy Foxmeyer for \$343 million—a lofty 35 times trailing net earnings—and assume the unit's \$260 million in debt. Simon and Chambers, the board's savviest members, voted thumbs down. They argued that Foxmeyer's premium price made it an imprudent investment. Both men resigned from the board soon after and sold their stake in NII.

The rest of the board went along. Love boasted that under Foxmeyer's outstanding management, NII's new core business would continue its strong growth. But by the summer of 1986 there was a price war within the drug industry. Beyond that, Foxmeyer was hampered by its own diversifications. An effort to sell hospital supplies was floundering; a project to sell computer services to druggists had to be canned. A move to put the 1,300-store Ben Franklin five-and-dime chain on Foxmeyer's computer system was a disaster. Foxmeyer's profits slid by 50%, ending the year at \$10 million. But Tauscher denies that he sold National Intergroup a bill of goods.

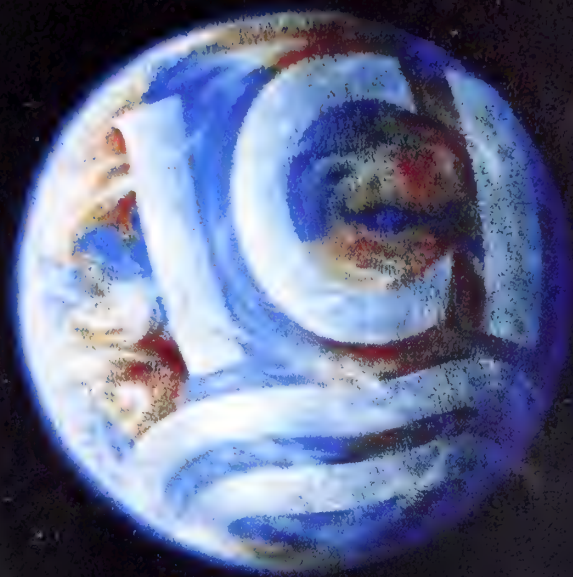
He blames Foxmeyer's problems largely on industry conditions. "Foxmeyer will do well in the long run for NII," he says.

Meanwhile, in February, 1986 Danforth, then chairman of Westinghouse, joined the board. Even though Westinghouse headquarters are just across the street, the companies were worlds apart. The folksy, no-nonsense Danforth was in the process of turning Westinghouse into a blue-chip stock by deftly shedding assets and pursuing niche acquisition. He was the only insider on an independent-minded 10-member board.

Love's board, by contrast, included four insiders. And eight of the 11 outsiders, among them sons of four wealthy Midwestern families, had social or business



FORMER WESTINGHOUSE CHAIRMAN DANFORTH "IS ON THE BOARD," SAYS ONE NII EXECUTIVE



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Medical
00000546-2 DONNELLY, MARY

Patient No: 000005462

Patient Demographic Data:

Last Name: DONNELLY

Street : 96 ELM STREET

Choices

- 1: Enter Diagnoses**
- 2: Enter Case Data**
- 3: Enter Consults**
- 4: View Charges**
- 5: View UR Data**
- 6: View Results**
- 7: View Guarantor**
- 8: Select New Patient**

Selection: █

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-Jay Rose, V.P.
General Manager
Trunk Systems
Division, SMS

links to Love or his father. There were old buddies like Charles T. "Chick" Fisher III, chairman of NBD Bankcorp Inc., parent of National Bank of Detroit and a descendant of the Fisher Body family; and Detroit's Joseph L. Hudson of the Dayton-Hudson Corp. department store clan. Directors R. L. Ireland and Richard S. Smith had ties to George Love: Ireland was a Hanna director, and Smith a former Hanna executive. A golfing buddy of Pete's, Smith also served as National Steel's vice-chairman until 1987. Then there was Sigo Falk, whose ties to National go back three generations.

Several directors socialized with Love, either hunting quail at his father's northern Florida plantation or golfing at the Laurel Valley Golf Club, of which Love is president. Hudson and Love went to President Bush's inauguration together. "They really like Pete," says a former director. "It got in the way of objectivity." Love insists that, on the contrary, his friends were "an asset" since they gave him frank advice. "Our board has been independent, inquisitive, after the facts," he says. Nearly all of the current and former directors who have served under Love declined to comment for the record, or could not be reached. Buck Mickel, former president of Fluor Corp. who joined NII's board in 1978, takes investor criticism "with a grain of salt," he says. "NII is an excellent, viable company...even though lots of problems have come out of the blue."

Though Danforth declined to be interviewed, sources say he immediately began asking low-key but probing questions at board meetings. He quietly told Love and Haas to watch Tauscher closely. With other directors, he privately pressed Love to cut back on civic activities. "Danforth is the board," says one NII source. "He was the only one who saw through Tauscher's bull—projections. When Tauscher got up to talk at meetings, Danforth perked up like a bird dog on point."

By early 1987, NII was slipping fast. "I was terrified," says one former director. Falling prices were squeezing oil. The

steel unit had operating problems, exacerbated by an expensive labor contract and cultural clashes with its Japanese partner. With \$600 million in debt and \$90 million in annual interest payments, NII was in technical default. The crisis prompted the board to sell half of Permian to the public. Love cut NII's \$20 million corporate overhead by 25% and eliminated most of his jet fleet. Still, Love's list of outside activities kept getting longer.

NII's bankers, led by Citibank, backed out of a new loan agreement as Tauscher's latest forecasts fell apart. "The poor credibility factor ended our



GEORGE LOVE, PETE'S FATHER, WAS VICE-CHAIRMAN OF NATIONAL

relationship," says a former lender. A new group gave new loans with stringent covenants.

Then came a succession crisis. An alienated Haas, 52, Love's one-time heir-apparent, wanted to leave. After an extensive search, Love spotted Farley, also 52, a chief financial officer who soared past Black & Decker's heir-apparent to lead the ailing company from 1983 to 1986. Son of a Joseph E. Seagram & Sons Inc. manager, Farley went to school at night to get a business degree. He rose through the ranks at RCA Corp., then to the top financial job at Conrail before going to Black & Decker.

Opinions about Farley are still divided at B&D. For his first year at the helm, he received high marks for a restructuring

that initially produced record results. But his star fell along with profits in his second year, and an impatient board wanted to oust him in favor of the charismatic Nolan D. Archibald, whom Farley just months before had hired as No. 2. Farley says he left voluntarily after it became clear that "a shoot-out with Archibald would damage Black & Decker's recovery."

Farley arrived at National Intergroup in February, 1988. By then, Love was ready to dump Tauscher. Months earlier, Tauscher hooked up with an ex-partner to buy ComputerLand Corp. and now was chairman of ComputerLand as well as CEO of Foxmeyer. He had other deals cooking, too. Before Love could act, Tauscher flew to Pittsburgh to tell Love he was leaving. He resigned in July.

NEW REALISM. While Love says he and Farley now operate as equals, bankers say that the soft-spoken Farley firmly took NII's reins immediately after joining the company. While Love had promised profits in the coming fiscal year, losses continue to mount. Farley pushed Love to take a write-down of a Luxembourg aluminum mill and omit the common dividends rather than refinance public debt. He also rounded up a new group of bankers.

Farley is shaping up Foxmeyer, too. It accounts for 85% of NII's \$3 billion in sales, and profit margins are half the industry average. NII's \$50 million second-quarter write-down covered Foxmeyer restructuring charges, and Farley wants to get rid of nearly all nondiversifications. "Farley brought a new realism to the company," says a lender.

Some investors are encouraged, but others don't want to wait for the hefty profits Love expects by the mid-'90s. After all, NII's latest quarterly profit came largely from the cyclical recovery in steel and aluminum, and Love put those units up for sale. So raider Hurwitz may offer investors a way out.

Hurwitz is a major partner of Walke Street Associates, a New York investment firm that has 8% of NII's shares. Hurwitz' Los-Angeles-based Maxxar Group Inc. also recently bought aluminum-maker KaiserTech Ltd. Speculation is that Hurwitz would like to break up NII and keep its prospering U.S. aluminum unit. Analysts think a breakup would fetch as much as \$40 a share.

That's why Hurwitz is a serious threat, and Love is plenty nervous. He even called a huddle with the board last month to figure out ways to fend off the raider off. But even if Love gets a reprieve, by his own admission the heady profits he has been promising since 1986 are still years away.

By Gregory L. Miles in Pittsburgh



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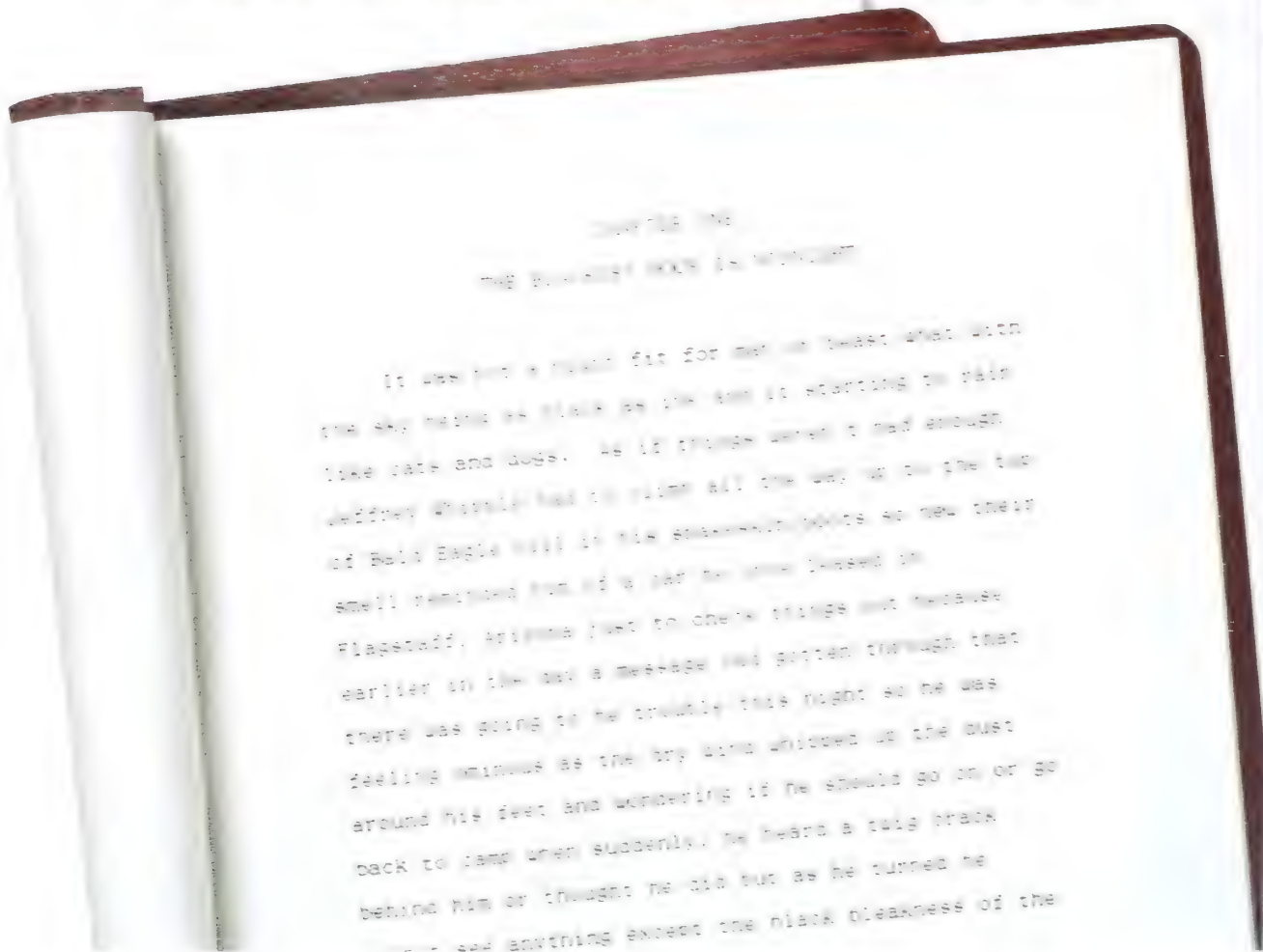
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ALMOST EVERYBODY WANTS TO BREAK UP SANTA FE

Chairman Krebs doesn't dismember it, someone else might



KREBS'S ASSET-RICH
COMPANY INCLUDES
ENERGY AND LAND

Talking with Chairman Robert D. Krebs about Santa Fe Southern Pacific Corp. is like having someone tell you the plot of a long-running movie. Here's the story so far: First, regulators in 1987 veto a proposed merger between the railroad arms of Santa Fe and Southern Pacific, prompting the ouster of Santa Fe Chairman John J. Midt. Then, Henley Group Inc. tries for 15 months to take over the company, only to be checkmated by a new shareholder, Canadian magnate Paul Reichmann. Finally, Henley slinks away after selling its stake to Itel Corp. and its chairman, Samuel Zell. In the end, Santa Fe borrows heavily to dole out \$4.7 billion to shareholders.

Even if that were not enough, Krebs promises even more thrills. "1989 will be just as exciting," he says. He plans to restructure what's left of Santa Fe, which last year had \$3.1 billion in assets from its railroad, mining, and real estate ventures.

Krebs fails to deliver on the excitement, his two biggest shareholders protest. *BUSINESS WEEK* has learned that Paul Reichmann, who sits on Santa Fe's board and whose conglomerate, Olympia & York holds 19.6% of Santa Fe stock, has requested that Krebs and other board members consider a complete

breakup of the corporation into separate rail, energy, and real estate companies. Investment bankers close to Olympia & York believe that within five years the pieces would be worth at least \$40 for each existing share of Santa Fe. That's well above the current price of Santa Fe stock, which has run up 36%, to a recent \$23, since early December. That's also way above what most analysts see as Santa Fe's breakup value. Neither Santa Fe nor Olympia & York would comment on this scenario.

Meanwhile, Itel's Zell, who controls 17% of Santa Fe, has hardly been idle. Zell, who dubbed himself "the Grave Dancer" because of his fondness for moribund companies, has approached big shareholders to discuss a sale of

their Santa Fe stock to him. Itel President Rod F. Dammeyer says Zell, also a Santa Fe board member, wants to boost his stake in Santa Fe to 20%. Itel, he adds cryptically, is mulling over "various strategic options" regarding its shares.

Krebs, a railroad executive at Southern Pacific before his rapid rise to the chairman's office at Santa Fe, declines to second-guess his two major shareholders. "Because they have a significant stake, they are spending a lot of time on the company," he explains. Krebs makes it clear he is open to any suggestions, even a properly financed outside bid.

PAY DIRT. There's plenty to tempt a raider, even after the sale of the Southern Pacific railroad to the Denver & Rio Grande Corp. Santa Fe owns 44% of one of the country's biggest oil pipelines. The company has large reserves of oil and gas, and its geologists recently struck gold in a Nevada mine.

Krebs may package these properties into limited partnerships, as he did with the pipeline. A rumor is brewing that Pennzoil Co. is interested in Santa Fe for its energy business. But a source close to Pennzoil Chairman J. Hugh Liedtke says he has his hands full with his stake in Burlington Resources Inc., a spinoff of Burlington Northern Inc.

Then there are Santa Fe's two biggest assets, its real estate and its railroad. Santa Fe controls almost 3 million acres, including a big piece of undeveloped land near San Francisco's financial district. Late last year, Krebs was ready to auction off some of those acres for an estimated \$800 million. But Reichmann stayed his hand and advised him to develop the land instead.

Santa Fe's biggest division, the \$2 billion rail system, is profitable, but its margins are below the industry average, and competition is relentless. "Every year the truckers gobble up more of the freight business," says Krebs. The company would like to wring some big concessions out of the unions, but Krebs doubts any major breakthrough in labor talks is imminent.

Krebs may try something dramatic with the railroad. He is working with consultants McKinsey & Co. to figure out which rail lines to sell off by mid-year. He even concedes that he might sell the entire railroad. One possible buyer, some institutional investors say, is Zell's Itel, which leases rail cars and operates some small railroads of its own.

As the rumors swirl, Krebs pursues his plans to satisfy shareholders. No matter what his grand strategy may be, Santa Fe's days as a railroad conglomerate appear to be over.

By Brian Bremner in Chicago and
Chuck Hawkins in Toronto

SANTA FE'S TREASURE TROVE

Business	Estimated selling price (millions)
Real estate	\$3,465
Oil, gas, gold & coal	2,054
Railroad	1,000
Cash & other	495
TOTAL	7,014
Less total debt	-3,120
BREAKUP VALUE	3,894

DATA: DILLON, READ & CO.

IS THE COMPUTER BUSINESS MATURING?

NEW TECHNOLOGY MAY NOT HALT AN EROSION IN GROWTH AND MARGINS

If you want to raise an eyebrow, tell a computer executive that the industry is maturing. Suggest that after 40 years of nonstop buying, the best customers have so much equipment they can't keep spending at historic rates. Note that amazing reductions in the price of raw computing power mean that demand must rise at least 20% a year just to keep the industry from shrinking. List some facts: Revenue growth is slowing, products are getting more standardized, margins are under pressure, consolidation is accelerating.

Then get ready for an argument. IBM dismisses the proposition out of hand: "Industry revenues can grow at two to three times the world gross national product—plus inflation—for as far as we can see," says Wirt M. Cook, director of strategy and business development. "There will be new uses and new users." Compaq Computer Corp. agrees. "You can get 25% annual growth for the foreseeable future," insists Michael S. Swavely, marketing vice-president.

Is this just wishful thinking from companies weaned on 20% and 30% annual growth rates? An increasing number of analysts think so. They're beginning to argue that the computer industry, which for 40 years has been the emblem of America's post-industrial prowess, is facing a fundamental change: The business that made folk heroes of baby boomers named Steve Jobs, Mitch Kapor, and Bill Gates is approaching middle age. "The industry is maturing," declares Norman Weizer, who follows computers for Arthur D. Little Inc. "We began to see it two or three years ago, but we didn't have the guts to say it until recently."

SLOW-GROWTH LIST. Here's the evidence: Annual sales growth for computer systems, in double digits just two years ago, has fallen below 10%; some say that by 1992 it may be as low as 6% (chart). Although this could be just a cyclical slowdown, many say it simply reflects the difficulty of wringing double-digit growth out of a well-established, \$100-

billion world market. While newer types of computers, such as PCs, still enjoy impressive growth, that isn't enough to offset slow growth in older mainframes and minicomputers. Prudential-Bache Securities Inc. analyst Rick Martin figures that 60% of the estimated \$169 billion in revenues recorded last year by the world's major computer makers—their combined sales with at least \$500 million in annual sales—came from older computer technologies. "No matter how fast the new technology markets grow," Martin says, "they aren't big enough to restore overall growth rates to double digits."

If the computer business is maturing, it may be the first time an industry has done so while its technology is still in its infancy. Rapid advancements in technology keep pushing down the cost of computing power. But, paradoxically, that's the industry's biggest problem. The ability to pack more and more power into smaller and cheaper packages every year means that computer makers have to run fast just to match last year's

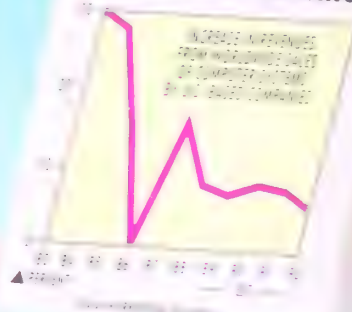
SIGNS OF AGING

Even though technological change in the computer industry is still accelerating, some key indicators show that the business is graying

WITH LESS INTENSE SPENDING ON COMPUTERS...



...THE INDUSTRY'S REVENUE GAINS ARE SLOWING...



nesses. IBM is a case in point: It's the leading player in personal computers, a market that's still growing 12% to 17% a year. But its PC revenues haven't compensated for a slowdown in mainframes and minis—a slowdown caused in large part by the success of the PC. As a result, IBM's revenue growth has averaged only 1% since 1984.

The same problem will eventually afflict even today's highest flyers. "Desktop systems, networking, and packaged software are all growing fast," observes William Krause, chairman of 3Com. "But they'll be maturing, too." 3Com's business, selling personal computer networks, grew 62% last year. But market research and 3Com's projections indicate that the market will cool off to a 10% annual rate by 1992. By then, says International Data Corp., growth in PC revenues will have dropped to just below 5%, adding the likes of Sun Microsystems, Apple Computer, and Compaq to the slow-growth list.

It's not sure, a wholly unexpected technological breakthrough could once more spawn some new sub-industry, like personal computers, that will stimulate a new wave of double-digit growth. Even without such a breakthrough, it may be too late into the next century—if ever—before computer-industry growth slows to the rate of such plodders as automobiles and steel. And for the next few years, demand in European and Asian markets promises to partially offset the slowing demand in the U.S. (page 74).

Still, a slowing trend is taking hold. What does, "chances are that the entire industry will be restructured," says Prue Martin. As suppliers try to grow by grabbing market share, consolidation is unavoidably spread. Eventually, pre-

dicts Robert J. Conrads, managing director with investment bank First Boston Corp., the industry may be ruled by less than a dozen huge Japanese and U.S.-based multinational suppliers that will have overwhelming advantages in manufacturing and distribution. Smaller players won't disappear. Many will survive as suppliers, like the parts companies that feed Detroit.

All these changes are likely to require a new style of management. The free-wheeling risk-takers and brilliant engi-

Eventually the industry may be dominated by fewer than a dozen huge Japanese and U.S. multinationals

neers who could blow opportunities and still be saved by soaring demand may no longer have the right stuff. "It used to be that you could take broad strokes at the markets, you didn't have to focus," says one computer marketing executive. "Not these days."

Indeed, marketing savvy, more than entrepreneurial skill, will be increasingly crucial as the industry shifts from selling chunks of hardware to installing networks. Such "systems integration" will require legions of skilled analysts and software specialists to customize systems. In short, the computer business will wind up looking a lot more like a service industry, and some of the biggest names may not even be computer makers. They could include Electronic Data Sys-

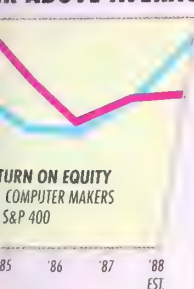
tems, Andersen Consulting, Computer Sciences, the Baby Bells—anyone who can mix and match hardware and software to satisfy a customer.

A lot of this hinges on what happens to corporate spending for computers—and these buyers are getting stingier. After adjusting for inflation, computer spending by the 1,000 largest corporations has tripled since the late 1970s, to 3% of gross revenues, according to IDC President Thomas Swithenbank. Already, outlays on computers account for more than 14% of the average capital budget. "Companies can't support more huge increases," Swithenbank adds.

NO MORE GEE-WHIZ. In particular, notes Michael Raimondi, an analyst with DRI/McGraw-Hill Inc., banks and insurance companies may no longer be reliable engines of growth for the computer industry. "They started early and became the biggest bloc of customers, buying \$13 billion worth of computers every year," he says. "But now the biggest segment no longer appears to be growing rapidly." Where they once increased computer spending by more than 20% each year, these companies are cutting back to between 5% and 10%, he says.

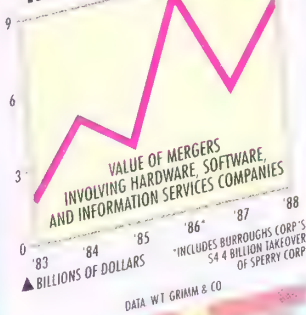
Spending habits are influenced by changes in the ways that companies use computers. They used to believe implicitly that computers would cut costs by automating office tasks. Now computers are part of a more defined—and measured—effort to improve manufacturing, distribution, and other operations. That means there's less tendency to buy technology for technology's sake. "We don't do much gee-whizzing anymore," says Lawrence E. Bacon, senior vice-president of Travelers Corp. "We make sure our expenditures on technology re-

PROFITABILITY IS NO LONGER ABOVE AVERAGE...

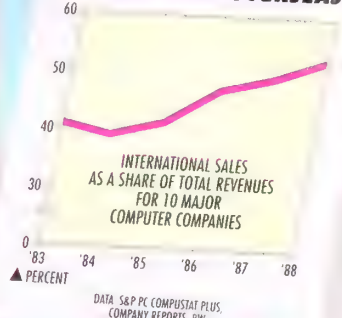


ALOMON BROTHERS

...CONSOLIDATION IS NOW A FACT OF LIFE...



...AND THE ACTION IS MOVING OVERSEAS





'THERE IS SATURATION AMONG MATURE CUSTOMERS IN MATURE TECHNOLOGIES. THAT'S WHY MAINFRAMES HAVE HAD SINGLE-DIGIT GROWTH FOR MOST OF THE 1980s'

—CURTIS A. HESSLER
Chief financial officer and executive vice-president, Unysis Corp.

turn something to the bottom line."

The more immediate hindrance to demand seems to be overkill: New products are flooding the market faster than customers can keep up with them. "The market is really baffled," says William Caffery, an analyst with market researcher Gartner Group. "The difficulty is absorbing what is already available—let alone what is going to arrive in the future," says Irwin J. Sitkin, vice-president for corporate administration at Aetna Life & Casualty Co.

Software is the major stumbling block. For years, programmers have been unable to crank out new packages fast enough for mainframe customers to get the most from their machines. Now, with multiple mainframes, dozens of minicomputers, and hundreds of PCs, customers are "overmipped." They have tremendous computing capacity as measured in MIPS—the power to process one million instructions per second. But "we don't have the software to fill the MIPS," says Robert C. Hughes, vice-president for industry marketing at Digital Equipment Corp. "The key is to get programs that are MIPS suckers." IBM's Cook says that in the 1990s complex "artificial intelligence" programs and software that manages digitized graphic images will use a lot more processing power.

But there's a catch: It has been possible to automate

the design of increasingly powerful hardware. Creating software, however, remains a laborious and slow undertaking. And the biggest MIPS suckers are the hardest to produce.

The gap is widest in personal computers. This year, PCs using Intel Corp.'s 80486 mainframe-speed microprocessor will appear. Yet almost no software exists that truly takes advantage of the hardware innovations Intel built into its 80286 chip—and that was five years and two generations of PCs ago. "I think we're on the edge of a backlash," says S. Jerrold Kaplan, a founder of artificial intelligence software developer Teknowledge and now president of GO Corp., a

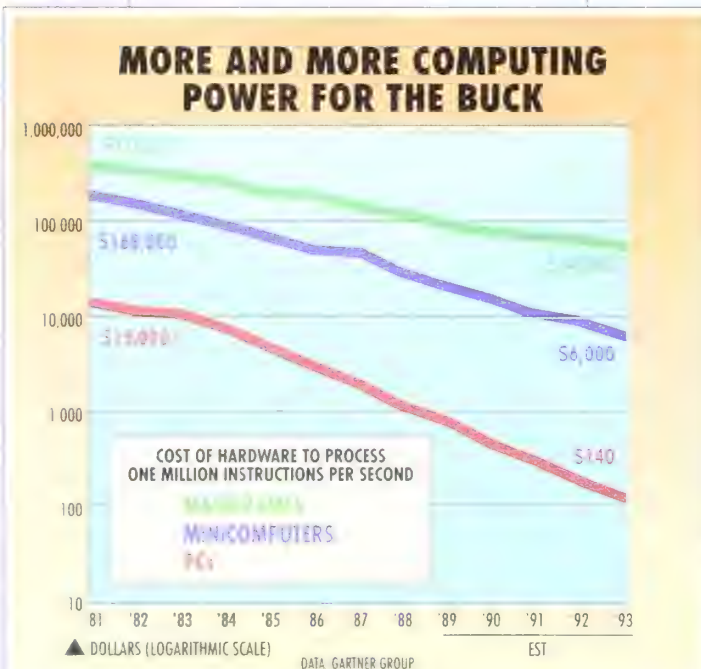
hardware startup. Kaplan and other industry executives are beginning to worry that disenchanted customers may limit buying until the software catches up with the new hardware. That will choke off the industry's biggest source of growth.

STREAMLINED. For now, however, customers keep buying PCs and other microcomputers because, even without advanced software, they're a bargain. Relentless improvements in chip technology have made it possible to pack the power of an early 1980s mainframe into a desktop computer costing \$5,000. Proponents of RISC, a type of streamlined computer design, claim it can cut the cost by another 84%. Robert Miller, president of MIPS Computer Systems Inc., a RISC supplier, says that this year computer makers will start selling \$5,000 desktop systems based on a version of a MIPS chip that can zip through 20 million instructions per second. That's almost the same speed as an IBM mainframe costing \$2.9 million.

So customers can now cut their computer budgets and still buy more computing power. The small machines are also cheaper to run, since they don't require air-conditioned rooms or squadrons of technicians to keep them going. Kera Co., a \$1 billion Boston maker of mechanical supplies, shifted 75% of its computer work from mainframes after it was spun off from Colgate-Palmolive Co. in a leveraged buyout last October. "Mainframe systems and PCs are the way to go," says Ron Cipolla, director of management information systems. "We're spending \$20 million a year, down from \$23 million two years ago, and we intend on pushing it down."

Additional savings may come from so-called desktop systems that rely on standardized software. The most computer makers have prospered with proprietary software that locked in customers who could switch brands only by spending a small mint on new programs. But after nearly a decade of buying dozens of different brands of PCs—using the same software—customers also want flexibility from bigger computers.

For instance, a standardized version of the Unix operating system, a basic framework of software that runs everything from workstations to supercomputers, may lure customers from the old ro-



ary trap. They'll be able to use the applications software, such as data programs, on lots of different machines with little reprogramming. Although Unix systems represent a small part of the market now, they are expected to account for nearly 20% of computer systems sales by 1992. Even Big Blue's most loyal customers are demanding open systems. "We, too, want to be open," declares Aetna's Sitkin.

In the short run, open systems mean open competition, and that means "hardware margins are going down," says Everett Ehrlich, Unisys Corp.'s chief economist. Where gross margins on mainframes and minicomputers can exceed 40%, margins on microcomputers are expected to fall to 20% or less. The effect on profits is clear: As desktop computers proliferated, the return on investment for 15 major producers listed by Salomon Brothers Inc. fell below last year's average for companies in the Standard & Poor's 400-stock index.

In fact, it's now a widely accepted view that, except for specialized machines such as supercomputers, hardware will tend to be a commodity. That's true of PCs, where Asian copycats have entered a mass market. But the phenomenon is spreading. "There will be a kind of creeping commoditization," says Kidder Peabody analyst William D. Easterbrook. "Even the huge machines now cost \$5 million or \$10 million will someday cost \$500,000 or less." Mainframe makers may be able to preserve high margins, but the lower revenues will

be offset by falling prices, commodity production, and slowing growth are all marks of a mature industry, as is stagnating technology. Another sign is that mature industries usually have higher barriers to entry. Yet computer technology is actually generating, and standardization is making the business easier to crack. The computer industry, it seems, is maturing on its own way. "There are no models for us," notes Kenneth Flamm, an economist who tracks high technology for the Brookings Institution.

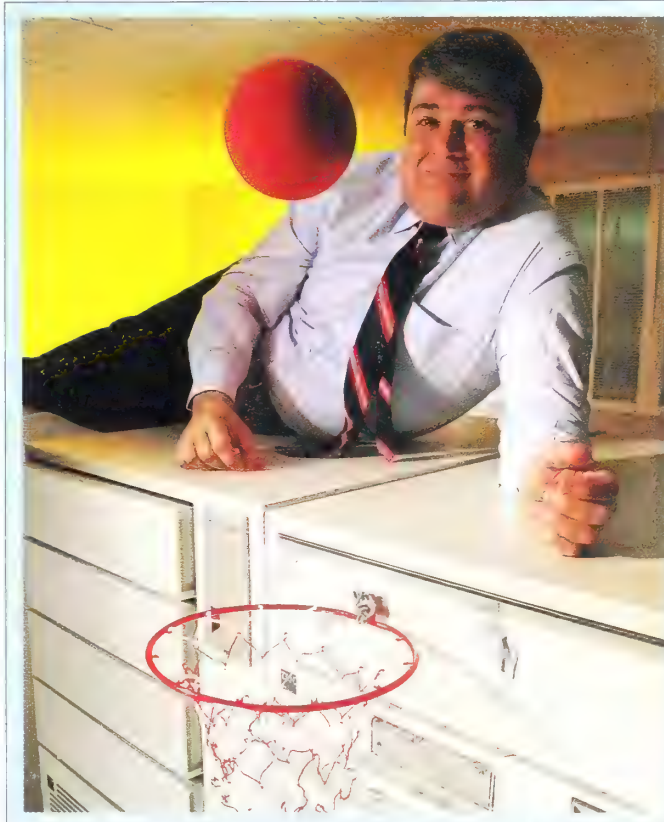
CHARTING A NEW TRAIL. Still, a pattern may be emerging. "Maturation and slower growth became clear to us soon," says Curtis A. Hessler, chief financial officer at Unisys, the product of the merger of mainframe makers Burroughs and Sperry. "There is saturation among mature customers in mature technologies. That's why mainframes had single-digit growth for most of the 1980s." By 1980 mainframes had become essentially a replacement business,

and IBM was picking off existing customers from Burroughs and Sperry. Unisys Chairman W. Michael Blumenthal decided the way to fight it was to get big enough to achieve IBM-size economies of scale—and move into faster-growing new technologies.

After the merger, Unisys shed 10,000 employees and plans to lose an additional 2,790 this year. By reducing overhead and duplicating operations, Blumenthal has boosted net earnings by 80% over the total earnings of Burroughs and Sperry in 1985, a gain that analysts say neither company could have accomplished alone. Unisys certainly hasn't got all it wanted—revenue growth was a feeble 2% in 1988, throwing into question

Cunningham, a former Wang executive, is trying to raise \$500 million for a computer-industry takeover and merger fund. "Five years ago the stock prices were too high," he says. "Now they've come down to the level that you can get operating efficiencies after a merger." Cunningham proved his point with Computer Consoles Inc., a money-losing minicomputer maker he turned around and then sold to Britain's STC PLC for \$168.4 million on Feb. 10.

Investment banks see the opportunity, too. Drexel Burnham Lambert and Merrill Lynch have pledged more than \$1 billion for a highly leveraged—and controversial—takeover bid by raider Bennett LeBow's MAI/Basic Four for Prime



'MID-RANGE SYSTEMS AND PCs ARE THE WAY TO GO. WE'RE SPENDING \$20 MILLION A YEAR, DOWN FROM \$23 MILLION TWO YEARS AGO.'

—RON CIPOLLA
Corporate director of management information services, Kendall Co.

Blumenthal's goal of making \$10 billion Unisys a \$20 billion company by the mid-1990s. Still, he may have blazed a trail.

In an era of slow growth "the industry will consolidate like crazy," predicts Marc G. Schulman of UBS-Phillips & Drew Global Research Group. Overall, analysts say, the industry has 20% excess capacity, a lot of it at midsize companies in the minicomputer business. With DEC and IBM gaining, and with PCs encroaching from below, companies such as Wang Laboratories, Prime Computer, and Data General are seen as candidates for mergers or restructuring. Second-tier players in the newer microcomputer markets may also become targets: Workstation maker Apollo Computer Inc. is rumored to be one.

So ripe are conditions that John Cun-

Computer. Kidder Peabody and First Boston both have active merger and acquisition programs in computers. Broadview Associates, a Fort Lee (N.J.) investment banker, has become a boutique for small deals, working with private companies that can't find a public market. "There are a lot of \$10 million and \$20 million companies that want to go public but can't," says John Dexheimer, a Broadview principal. So they merge.

The key to many mergers won't be technology or economies of scale, however. Says Conrads of First Boston: "The real value is in the distribution"—a company's thousands of customers and field organization for reaching them. Some investment bankers think Japanese computer makers might choose this path for their long-awaited push into the

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BANKS RECEIVE BILLIONS
ON ONE COMPUTER

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COMPUTER SALES HAVEN'T LOST THEIR SIZZLE OVERSEAS

If this is maturing, Compaq Computer Inc. could stand more of it. Last year its European sales zoomed by 150%, to about \$750 million. At Christmas, when its new factory in Scotland fell behind, Compaq chartered four cargo jets to ship in extra supplies.

Is this industry approaching middle age? Actually, it makes sense. If growth at home is slowing, computer makers should head "over there." They are. In 1988, for instance, IBM Corp.'s international volume jumped 15%. At 57% of total revenues, that accounted for virtually all of IBM's 8% sales gain, to \$59.7 billion. The trend was similar for Digital Equipment Corp. and Hewlett-Packard Co., among others.

Foreign customers are buying like mad. In Europe, where everyone is preparing for Continental free trade in 1992, overall computer sales grew 10% last year, 43% faster than in the U.S. Sales rose 14% in Japan and up to 20% in the rest of Asia. Analysts say that total European sales could surpass America's by the mid-1990s. Already

dence on the likes of IBM and DEC.

Sun is No. 1 in Japan's admittedly tiny workstation market and is vying for No. 1 in Europe. It has signed licensing and marketing deals with large foreign companies—what CEO Scott McNealy calls "country makers" because of their local clout. These include Britain's ICL, France's Matra, South Korea's Hyundai, and Japan's Fujitsu, Toshiba, and Seiko Instruments.

LOCAL APPROACH. This is risky. The country makers may compete with Sun. And the Japanese tend to reverse-engineer U.S. products, or make their own versions to compete with their former partners. Still, Sun and other U.S. workstation makers have a big lead. Sun is headed for a 60% sales increase to \$1.8 billion in the year ending this June, more than 40% of the total from abroad. McNealy expects that figure to eventually hit 65%.

Every company has a different approach. DEC adapts to the local culture. Its European sales quadrupled in five years, to \$4.2 billion, and it has created

new competition from overseas rivals.

Two big names are West Germany's Siemens, which has \$13 billion in cash and Italy's nimble Olivetti. Already the European Commission and national governments are spending heavily on cooperative programs such as Eureka, an R&D project, to help the home industries compete. The Europeans may even merge into two or three big groups and buy small U.S. companies with good European positions and advanced technology.

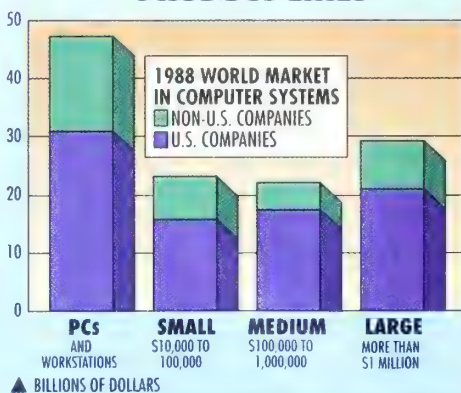
Asia could also turn into a battleground for U.S. producers. IBM, Unisys, and DEC have a lock on sales in Korea, Hong Kong, Singapore, and Malaysia. But in Japan, the key market in Asia, Fujitsu shoved IBM into second place in 1979. IBM has slashed mainframe prices to stem Fujitsu's gains. And it has inked 18 marketing joint ventures with Japanese companies. Analysts say IBM's sales in Japan rose 13% in 1988, to \$9.4 billion.

But other U.S. companies are lagging. Apple Computer Inc. has gone through four managing directors in five years while its revenues in Japan have languished. Its early products "were unable to handle the Japanese language adequately," says Shaw Hori, Apple's vice-president for marketing in Japan. He adds: "The company was growing so quickly in the U.S. and Europe, it couldn't support a worldwide business." Now headquarters is investing in marketing and dealer incentives and improving Apple's basic software for computers sold in Japan. And recently, Apple set up an R&D

U.S. COMPUTER MAKERS' SHARE OF WORLD MARKETS...



...AND THEIR BIGGEST PRODUCT LINES



pan-European, the major U.S. computer makers are well placed to take advantage of this. More so, ironically, than such rivals as Siemens, Nixdorf, ICL, and Olivetti, who are strongest only in their home markets.

Now U.S. producers are trying to pad their lead. From its beginning, Sun Microsystems Inc., the seven-year-old Mountain View (Calif.) maker of workstations, has sold products that appeal to international tastes. It used Unix for its basic software, an "open" operating system that lets customers avoid being locked into one supplier. That's key overseas, where customers fear depen-

dence on the likes of IBM and DEC. There are some ifs, however, about how long U.S. computer makers can depend on Europe. The dollar has inched up recently, and most analysts argue that computer sales will slow when the 1992-related buying spree ends. Beyond that, the U.S. faces

a "distributed headquarters" to manage that growth. West Germany handles marketing, training, and software services for manufacturing customers, while France handles telecommunications. DEC scores political points by giving each country some high-skilled jobs. And since Europeans don't like to move, hiring is easier.

team for new Japanese products. U.S. executives say they could handle these challenges more easily without pressure from Wall Street. European and Japanese producers often settle for 3% to 5% net margins, vs. the 8% returns U.S. markets want.

For U.S. computer makers it's a difficult position but not a hard choice. As their industry matures, they'll have to compete everywhere—in Osaka and Munich as well as in their backyard.

By Thane Peterson in Paris, with Jonathan B. Levine in San Francisco, Neil Gross in Tokyo, Leslie Helm in Boston, and Geoff Lewis in New York



**'WE HAVE A VERY
AGGRESSIVE
MANAGEMENT TEAM
LOOKING FOR WAYS TO
FILL THAT PIPELINE AND
MAKE US THE LOWEST-
COST PROVIDER'**

—ALBERTO GUDE
*Vice-president for
information services,
Enron Corp.*

estic market—bailing out slow-grow-
U.S. suppliers.

adds up to unprecedented pressure
mid-sized producers. "Computer com-
es can go two ways," says Ehrlich
nisisys. "They can attempt to become
-service, international players, or
can become subsuppliers to the big
s." The middle ground—\$500 million
perhaps \$10 billion in sales—is in-
singly untenable. Even Apple Com-
er Inc. and Sun Microsystems Inc.
afraid of tarrying there too long.
le Chairman John Sculley's goal is at
t to double his annual revenues, to
billion, in the early 1990s. And Sun,
ite a spectacular climb to \$1 billion
ales in less than six years, is sacrific-
margins now to gain the market
e it needs to survive a shakeout that
Scott McNealy predicts for the
s. "Only paranoiacs who go after
ket share will succeed in the long
n," he says.

ULTIMATE SOLUTION. The survivors, by
nition, will be much better managed.
"value added" and margins will
t to software, support services, and
ems integration. "You'll be able to
the same type of hardware from a
usand suppliers," says Hugh J.
ch, an NCR Corp. vice-president. "So
re will be tremendous competition to
ke computers more useful."

hat's why in the past three years IBM
undertaken a massive redeployment
prepare for the 1990s. It closed five
nts last year and cut its worldwide
roll by 20,000 positions, to 387,000
loyees. The composition of the re-
ning work force has been reordered.
e company expects to derive 30% of

its revenues from software in the 1990s,
up from 13% in 1988. Some 26,000 U.S.
employees are now working on soft-
ware, up 23% since 1986. Another 6,500
have been shifted into field sales and
support. And 6,000 have been added to
systems integration.

"The push is coming from customers
who want increasingly complex applica-
tions of technology," says David Creed,
corporate manager of systems integra-
tion and professional services at DEC,
where he directs 20,000 programmers
and consultants. "But they don't want to

**Maturity will separate the
winners from the losers:
'Growth can no longer cover a
multitude of sins'**

be in the business of implementing these
complex systems themselves."

Perhaps the ultimate solution is that
found by Enron Corp., an \$8 billion gas-
pipeline company based in Houston. It
has ambitious plans for using informa-
tion systems to maximize the use of its
pipelines, the way on-line reservations
systems have helped airlines fill capaci-
ty. But tackling that expansion and
keeping up with its other information-
processing needs seemed daunting. So
Enron has signed a 10-year contract
with General Motors Corp.'s EDS subsid-
iary to take all this work—as well as
Enron's 600 data processing employ-
ees—off its hands. For an undisclosed

annual fee, EDS will run Enron's infor-
mation systems and, with help from sys-
tems integrator Andersen Consulting,
will also develop new applications.

"We have a very aggressive manage-
ment team looking for ways to fill that
pipeline and make us the lowest-cost pro-
vider," says Alberto Gude, Enron's vice-
president for information services. "This
will help us accomplish that—and we'll
save \$100 million in the process."

Systems integration, however, is no
panacea for computer makers, says
Douglas R. Wilder, of Input Inc. He sees
it as purely defensive—"to protect their
hardware base." Although systems inte-
gration is expected to grow at a 31%
annual clip, yearly fees will amount to
only \$8.9 billion in 1993, according to
Input. Worse, if past experience is any
guide, this people-intensive work will be
less profitable than hardware.

WINNERS AND LOSERS. That's just one
headache facing managers in the matur-
ing computer industry. These days, con-
sultants at McKinsey & Co.'s electronics
practice are spending lots of time help-
ing computer makers come to terms
with such issues. They're teaching eight
techniques for "differentiating within a
standard." They preach cost-cutting and
better manufacturing efficiency. And
they stress reorienting R&D to advanced
software and away from basic hardware
design—which will be largely deter-
mined by chip manufacturers. "There
will be growth, and there will be innova-
tion," says McKinsey principal Michael
Nevens. "But in the 1990s you're just
going to have to learn to be a lot smart-
er. You've got to out-execute."

That's what will separate the winners



Hitachi's wide-ranging automotive technologies include car audio, the Satellite Drive information System featured on Nissan's CUE-X concept car and a microcomputer engine control system

AUTOMOTIVE

Automobiles should be more than safe, comfortable machines. They should also be able to communicate with the world around them.

Recent advances in car electronics technology have been remarkable. They've not only improved basic functions such as engine control, they're now being seen in man-machine interfaces providing more comfort and operating ease, and even in communications with the surrounding world. Down the road there are things even more exciting.

Hitachi's scientists and engineers are at work on a Multi Information System using a thin film transistor LCD to display operating information, road maps and a navigational system using these maps. With this system a driver could obtain a variety of driving information simply by touching the display screen. Eventually, he'll be able to use verbal commands to, for instance, regulate the temperature within his car. Hitachi electronics and semiconductor technology can also bring free communication to the outside and determine a car's

exact location through use of Global Positioning System satellites.

Hitachi has also developed a highly acclaimed hot wire air flow sensor used in engine management. It helps achieve the diametrically opposed goals of maximum power and fuel economy. And we've created many other superior products for driving control, suspension control, air conditioning and audio.

We link technology to human needs; and believe that our special knowledge will create new, highly sophisticated functions that are also easy to operate. Our goal in automotive electronics — and medicine, energy and consumer electronics as well — is to create and put into practice innovations that will improve the quality of life the world around.



HITACHI

Hitachi, Ltd. Tokyo, Japan

from the losers. For 40 years, each new wave of technology unleashed vast demand. All a computer maker had to do was catch the wave. No longer. Improving chip technology has shortened product cycles to the point where a delay of a few months may kill a new computer. As Apple may have just discovered with its widely publicized price hikes and subsequent sudden rollbacks, uncompetitive

pricing can sour a market. And misjudging a market's direction will be fatal. "Growth can no longer cover up a multitude of sins," says Martin of Prudential-Bache. Adds IBM's Cook: "We have to continue to improve all parts of our business to be competitive."

For computer makers, such changes will make the 1990s a cold world, indeed, compared with the era that is passing.

But the next few decades can also be more rewarding for the industry and customers. Rather than focusing on machines, both may at last concentrate the jobs the machines are capable of doing. When that happens, the long-awaited benefits of the "information age" will finally appear.

By Geoff Lewis in New York, with bureau reports

WHERE VENTURE CAPITALISTS ARE PLACING THEIR BETS



DIGITAL F/X CHAIRMAN MAYER: CREATING MULTIMEDIA SPECIAL EFFECTS PULLS IN FUNDS

If there's one place where the idea of a maturing computer industry seems truly heretical, it's in California's Silicon Valley. That's where venture capitalists still scan the horizon for billion-dollar opportunities. "We're all looking for the next big invention," says John W. Bayless of Sevin Rosen Management. "We've just scratched the surface," adds John L. Doerr of Kleiner, Perkins, Caufield & Byers. "We'll see more Apples and Compaqs."

Venture investors are still plowing substantial sums into computers and communications companies. The flow represents a smaller chunk of total venture funding—35% in 1987 vs. 55% in 1982. But the \$1.37 billion that went to computer companies in 1987 is near the 1984 peak, according to Venture Economics Inc. So where are the money-men placing their bets?

Many believe that helping computers communicate better will spur demand, so they're backing companies that will help PCs and workstations do more in networks. NetFrame Systems Inc., of Sunnyvale, Calif., is developing a "net-

work server" to synchronize the flow of information among scores of workers. Network Computing Devices Inc. in nearby Mountain View builds network terminals that resemble \$5,000 engineering workstations but sell for half the price.

PAPERLESS PAD. Investors also are hoping that a major software hit will spur network sales the way that Lotus 1-2-3 helped sell the original IBM PC. So startups are writing "groupware." A program being written by WorkFlow Systems Inc. is intended to guide electronic documents among workers performing routine administrative tasks. If it clicks, groupware "will put computers on desks that never had a reason to have them before," says WorkFlow President Tony Kobine.

Or in places they have never been—like inside briefcases. Although laptops are hot sellers, Dynabook Technologies Corp. thinks the smaller notebook-size PC it plans can do better. Founder Dan Wilkie says many buyers avoid laptops because they're too big or have poor screens. Licking those problems, he

says, will bring "an exploding market."

Another plan to draw more people to computers is to make PCs communicative on human terms. That's the idea behind GO Corp., which is said to be working on a tablet-size PC that recognizes handwriting. "Bridging the gap between paper and electronics is one of the great challenges of the 1990s," says President S. Jerrold Kaplan.

And in the age of MTV, what could be more natural than "multimedia"—the combination of computers, stereo sound, graphics, and video? One of the most ambitious multimedia startups is Digital F/X Inc. The Mountain View company's \$120,000 computer can handle all the editing special effects that video houses now do on equipment costing as much as \$1 million. Within three years, the company expects its machine's price to drop below \$50,000. Eventually, the processor is expected to fit into desktop PCs. "We're not doing this to be a niche player," says Digital F/X Chairman Steven T. Mayer. Nor are backers Intel Corp. and Apple Computer Inc., both of which want their computers to be multimedia machines.

TEAMWORK. Clearly, venture capitalists aren't easily discouraged. Despite software hangups, they continue to fund startups in "massively parallel" computers. By ganging thousands of microprocessors, such machines may someday produce extremely powerful computers at relatively low prices. In a recent entry, MasPar Computer Corp. is designing a system that it is expected will be capable of processing billion instructions per second.

Will any of these projects push U.S. computer growth back into double digits? None seems to have that potential yet. But Doerr warns against ruling out anything. He remembers when he was a young marketing manager at Intel. Nobody predicted that something called a microprocessor would spark the \$35 billion-a-year PC industry.

By Jonathan B. Levine in San Francisco

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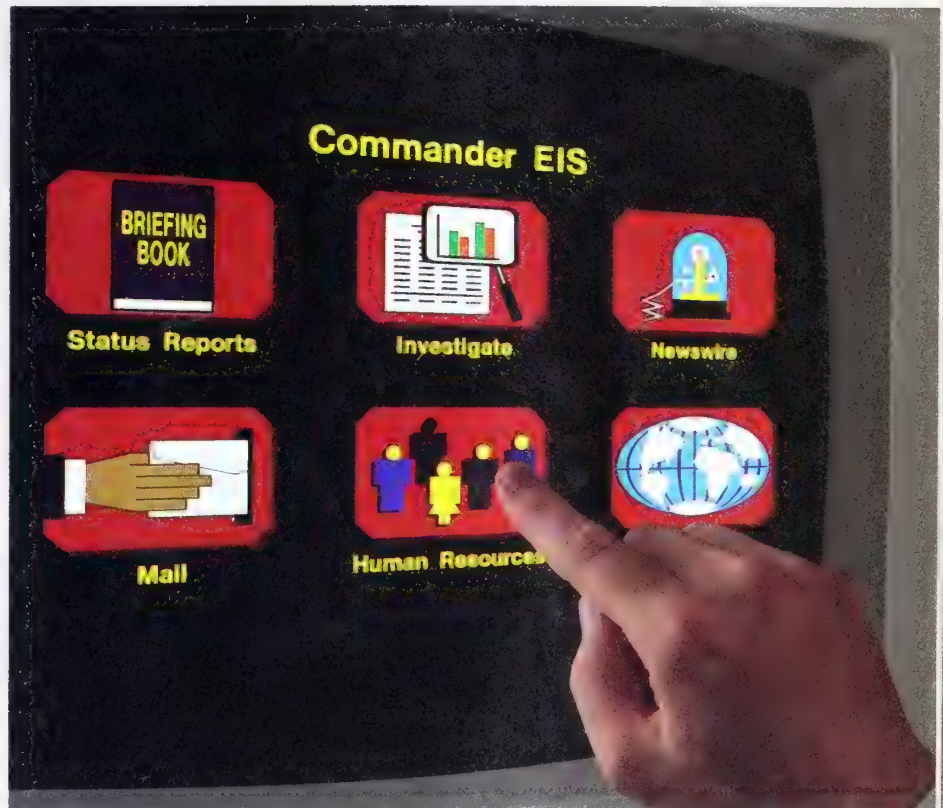


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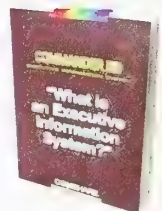
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*International Data Corporation, Decision Support and Executive Information Systems, Markets and Trends, Nov. 88 and Bus. Intentions for Decision Support Systems, Oct. 88 studies.

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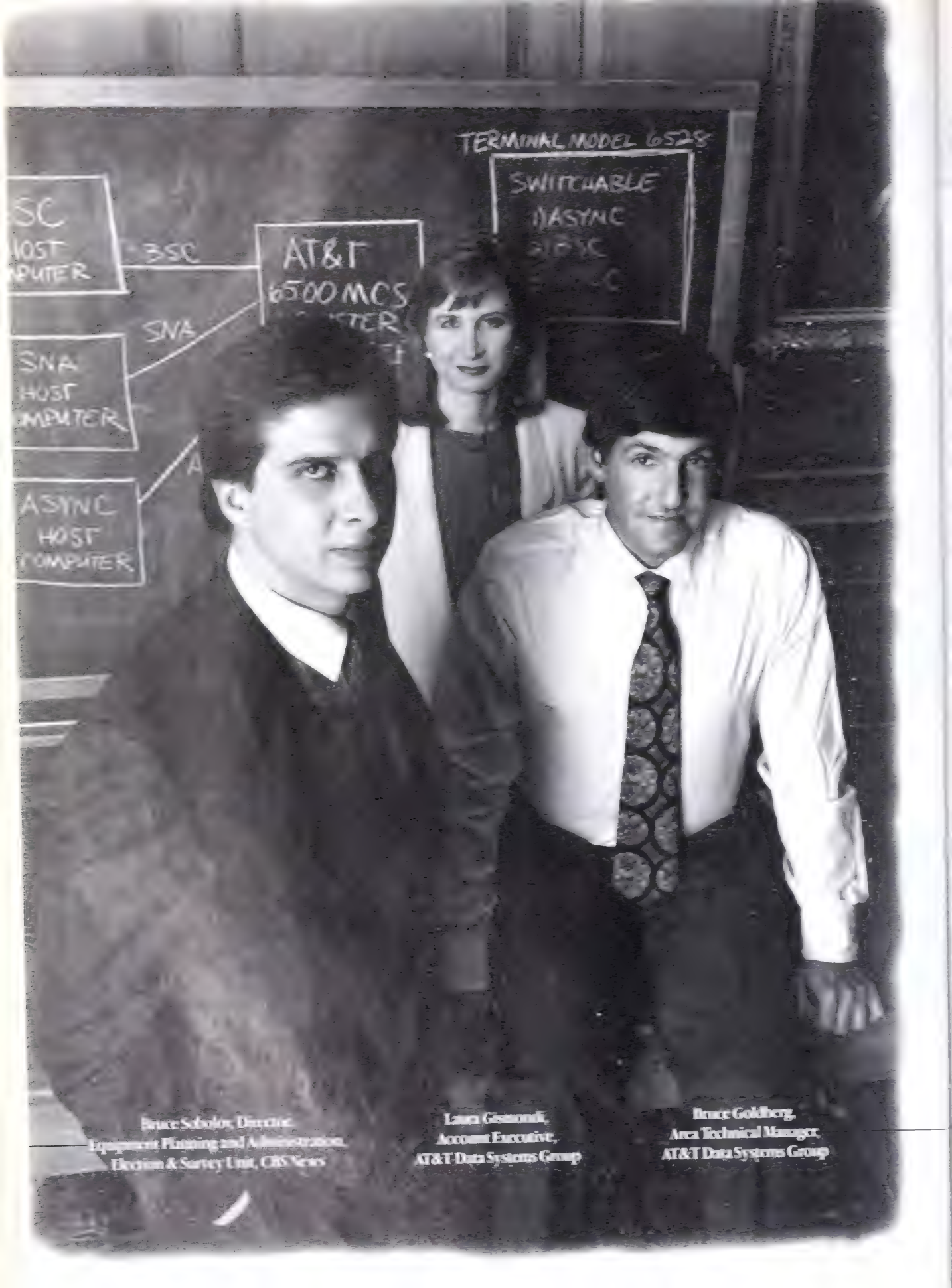


Commander EIS runs on IBM mainframes using VM/CMS or MVS/TSO operating systems; and DEC VAX/VMS. Commander EIS Executive Workstations run on IBM PC AT, PS/2 and fully compatible computers with EGA and either a mouse or a touch screen.

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Bruce Scholer, Director,
Equipment Planning and Administration,
Electron & Survey Unit, CBS News

Laura Gismone,
Account Executive,
AT&T Data Systems Group

Bruce Goldberg,
Area Technical Manager,
AT&T Data Systems Group



Bruce Sobolov of CBS News, Laura Gismondi and Bruce Goldberg, AT&T, savor the afterglow of their own post-election victory. They take us behind the scenes for a glimpse at some of the reasons why CBS was successful on election night.

FEBRUARY 15, 1989

AT&T: Afterwards, the critics said CBS was the best, the fastest.

CBS: Right, but we sweated it out for more than a year. With more 20-hour days than I care to remember.

AT&T: Your situation was pretty complicated.

CBS: We were faced with election projections, exit-poll analysis, and other studio programming applications running on IBM hosts.

AT&T: Plus the NewStar system we tied in with our wide-area network, ISN. It's distributed networked computing. Hey, we thrive on this stuff.

CBS: We're impatient around here. Speed is the only way you succeed with election coverage. The first thing we did was provide multi-host access with the 6500 System. Last election, everybody who needed access to two systems used two terminals. Twice the space, twice the cable, additional controllers, added expense, and wasted time.

We had programmers working simultaneously on three host applications, two bisync, one SDLC. They were constantly skating between terminals, wearing ruts in the rug. Now they have access to multiple sessions simultaneously from one terminal.

AT&T: The data moves over twisted pair, the same type wiring the technicians pulled for your System 75 PBX. That made sense.

CBS: An added advantage was having the same dedicated AT&T technicians installing and maintaining our system, providing consistency to my operation.

AT&T: But really, Bruce, why us?

CBS: Your responsiveness. At

custom host software we always used. We greatly reduced our cost.

AT&T: The other networks are watching, thinking, "How come CBS has the results already and we don't?"

CBS: It was a good night for us. Now the name of the game is streamlining for 1990. We're talking about a networked computer solution as a gateway into different host systems.

AT&T: With the AT&T Systems already up, running, and in place, we can almost completely automate your survey system.

CBS: That's a real big plus for all of us.

AT&T: Something tells me I've seen that same glint in your eye before. (Laughter)

Skating between terminals put ruts in the rug.

CBS, we all agreed that what we needed was someone who could deliver it fast, install it, test it, and support it. And you were hungry. You never said, "No, we can't do it." And you never took long to say "yes."

AT&T: You had computer networking problems. Solving them is the house specialty.

CBS: We do distributed computing to the nth degree. Our reporters are all over the country. They call in their results when the precinct closes. Before, we had over a hundred operators standing by, with phones and terminals. That election night we introduced the voice response system running on AT&T PCs.

AT&T: How many calls?

CBS: Thirty, thirty-two calls at once, reporters everywhere having voice response conversations with the IBM host. And all done with the same

The CBS Solution:

THE CHALLENGE:

Integrate IBM and DEC host computers and NewStar editorial system. Build an advanced computerized voice response system to speed election-night projections.

THE SOLUTION

AT&T 6500 Multifunction Communication System with multi-host sync/async 6529 terminals. AT&T CONVERSANT® Voice System for advanced communications running on AT&T WGS computers. AT&T System 75 PBX. AT&T Information Systems Network (ISN), a wide-area network.

THE RESULT:

CBS News provided fast, accurate election coverage throughout Campaign '88. The *Baltimore Sun* reported that, "CBS was recording results in all sorts of key races faster and with far more authority than either of the other networks."

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THE SLAM-DUNK COMES TO SMALL-TOWN AMERICA

The Continental Basketball Assn. is starting to score

It's game time for the Rockford Lightning. Spotlights zoom around courtside, and out prance the Lightning Flashes, the team's pom-pom squad, in a flurry of gold sequins and bleached blond hair. Next, the mascot, Lucky the Lightning Bug, sprints out, followed by the team. The 3,400 fans on hand seem amused by the hype, which includes a half-time promotion of kids shooting hoops for prizes. Later, when urged to wave their orange Lightning hankies, few respond. Cracks one fan: "Whoa, that's some sea of orange."

Welcome to the Continental Basketball Assn., 12 minor-league clubs catering to small-town America and aiming for big bucks. Once a tattered, carnival-like league with teams romping from one high school gym to another, the CBA is now winning some respectable crowds in the likes of Rockford, Ill., and La Crosse, Wis. League attendance last season rose 30%, to just over 1 million, or about what the new Charlotte Hornets of the National Basketball Assn. will draw this year. The idea is to play in small, sports-starved markets and charge a modest \$5 to \$10 per ticket. "We need to be the primary sports team in town," says CBA Commissioner Jay Ramsdell.

The CBA has also won the attention of the NBA, which called up 24 CBA players in 1988. NBA teams do not have farm clubs, so when an NBA player suffers a major injury, the team with the vacancy on its roster has the contractual right to select a player from any of the CBA teams, which have 10-man rosters. For the player called, it's a consummation to be wished. The maxi-

mum salary per team allowed by CBA rules this year is \$80,000. NBA teams can pay their 12 players \$7.3 million total. The minimum salary for an NBA player is \$100,000. Says NBA Commissioner David J. Stern of the CBA: "They've become our triple-A minor league."

Later this year, CBA owners will be pressing Stern to put his money where his mouth is. The three-year, \$1.8 million



DURING HALF-TIME THE KIDS SHOOT HOOPS FOR PRIZES

player-referral contract that the NBA has with the CBA expires in 1989, and Continental owners, who split the pot evenly, want to double the amount of money. Stern is mum on whether the NBA will cough up more money, but he's clearly impressed with the quality of play. "They've made things very appetizing for us," he says.

Investors seem to be hungry for franchises, whose values have soared in some markets. A decade ago owners paid \$8,000 a pop. But rights for league's three expansion clubs—set to premiere next year in Grand Rapids, Mich., Sioux Falls, S. D., and Columbus, Ohio—went for \$500,000 each.

Even in the smallest towns, investors see potential gems. Consider the case of Thomas Rubens, a Chicago commodities trader. Last year, Rubens organized a limited partnership of 30 investors to launch the new CBA team in Grand Rapids, population 187,000. Rubens is betting that the city is desperate for a basketball team.

'BRUTAL BUSINESS.' With proper packaging and marketing, CBA teams can pull in decent crowds and corporate sponsorship, contends Steve Lesnik, a Chicago-based sports marketer who has acquired the rights to the expansion team in Sioux Falls. He figures his new team, once established, can generate a gross profit margin of up to 20%, thanks to extremely low player salaries. Perhaps. But so far, easy money has been elusive for most clubs. And while the league's growth has been outstanding, only a handful of teams are now profitable. "Everybody thinks owning a team means money, but this is a brutal business," laments Rockford Lightning owner Jerry Frank.

It's also tough for the players, who must tolerate minor-league life for a crack at the NBA. The CBA offers them the chance to polish their game and show their stuff in front of NBA scouts. An outstanding example is Rickey Gunter, now playing for the Charlotte Hornets. He was the first-round draft pick in 1987 of the Golden State Warriors in the first round but was subsequently dropped. He then played for the CBA's Billings (Montana) Volcanos, making it back to the NBA with the Utah Jazz in 1988. In 1988, he was on the NBA all-star team. The fortunate have the option of going to Europe. "If I don't make it back to the NBA this year, I'm going to Italy. I can make about \$160,000 over there," says David Wood, a Lightning forward and former Chicago Bull.

With the lure of big money over the years and the rate at which NBA players sustain serious injuries, it's hardly surprising that player turnover is high with CBA teams. Indeed, many teams lose a portion of their starting roster by yearend.

Still, the fans don't seem to mind. In towns such as Rockford, where the game is the only game in town. It may be the superstar glitz of the big time, but it doesn't tell that to the Lightning Flashes.

By Brian Bremner in Rockford, Ill.

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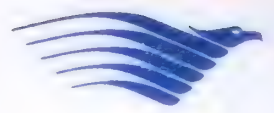
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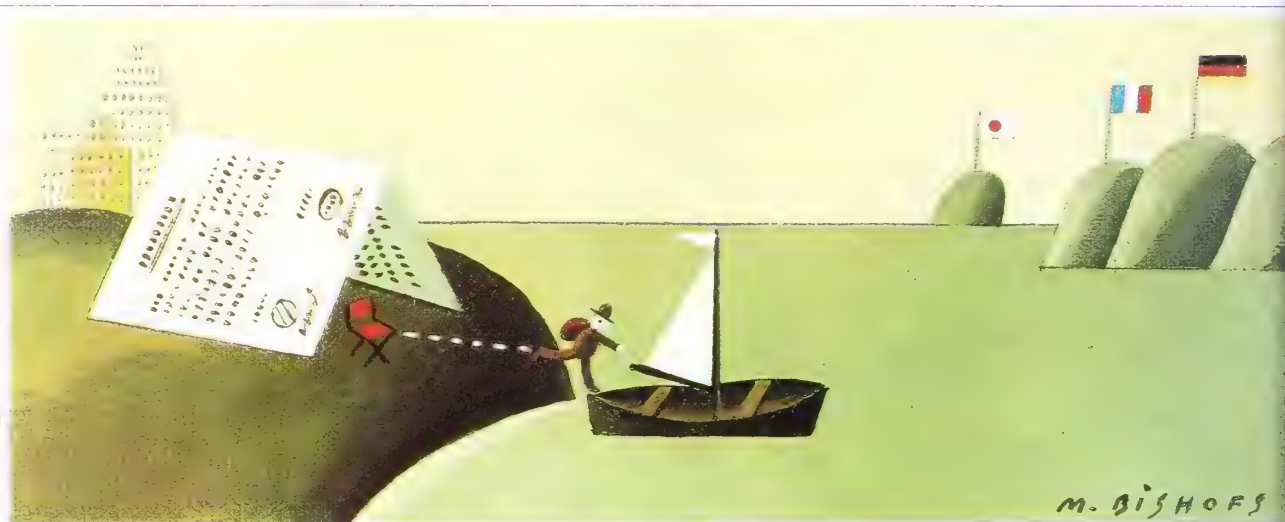
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WHO'S THAT KNOCKING ON FOREIGN DOORS? U.S. INSURANCE SALESMEN

Dozens of companies go globetrotting—even as banks and brokerages come limping home



The U.S. savored what seemed to be a small victory on the trade front on Feb. 13. It didn't involve a mainstay like beef or steel, but something that the U.S. has hardly ever tried to export—insurance policies. After years of hard bargaining by trade negotiators and insurers alike, five U.S. companies got the green light from the South Korean government to compete in that controlled economy for the consumers' insurance dollar. That brings to seven the number of American insurers licensed to do business in South Korea.

It's a story that will be reenacted many times in coming years. Dozens of U.S. insurance companies, including Prudential, Equitable Life, and Connecticut Mutual Life, are aggressively trotting the globe for new markets. And they're doing so even as many banks and brokerage houses come limping back from crowded markets abroad. Why try? Because the American market is saturated—particularly in life insurance. "Profit margins in the U.S. have been driven down to the point where you are not sure whether making more sales is a good idea or not," says Dennis F. Mullane, chairman of Connecticut Mutual Life Insurance Co.

That's the immediate impetus for the industry. For the nation, though, success could help the balance of payments; like merchandise trade, the financial services

sector is in the red. A lot depends on whether U.S. financial companies can attain the critical mass necessary for survival in an increasingly international market.

The U.S. accounts for 40% of the nearly \$900 billion in premiums the world's insurers collected in 1986, the last year for which good international data is available (charts). But the elbow room for profitable growth lies abroad. In many of Asia's newly industrialized nations, the age of the insurance consumer is just beginning. "Disposable income is reaching levels among large numbers of people who are now in a position to consider the insurance option," says Gordon J. Cloney, president of the International Insurance Council.

In the European Community, where the last trade barriers are to come down by 1992, U.S. insurers sense enormous pent-up demand for the more competitive policies they could provide. In France, a basic life insurance policy

costs about two-thirds more than in actively free-wheeling Britain. In Poland, insurance is priced an astonishingly times higher than in Britain. The European insurance markets tend to be fragmented, with local rules governing premiums and policy terms, and discouraging cross-border competition.

OLD HAND. Creating it will take more than knocking on doors. Foreign insurers aren't going to give up their comfortable turf without a fight. And they know the streets. In contrast, most U.S. insurers have ventured abroad only to serve their big corporate clients. They draw a scant 2% of their revenue from foreign business. Even if they can overcome cultural differences and regulatory hurdles, it may take years of hefty expenses before profits—if they start rolling in. Prudential Insurance doesn't expect its new Japanese subsidiary to show a profit until 1995.

Certainly, U.S. insurers are retooling themselves for the new European market. Connecticut Mutual has set up a Paris-based company, CM Transatlantic, to sell life insurance to the French. American International Group, the few old hands abroad, is restructuring its \$500 million European presence and casualty insurance operations, merging most of its operations into a new company, Paris-based UNAT, replacing 13 different national

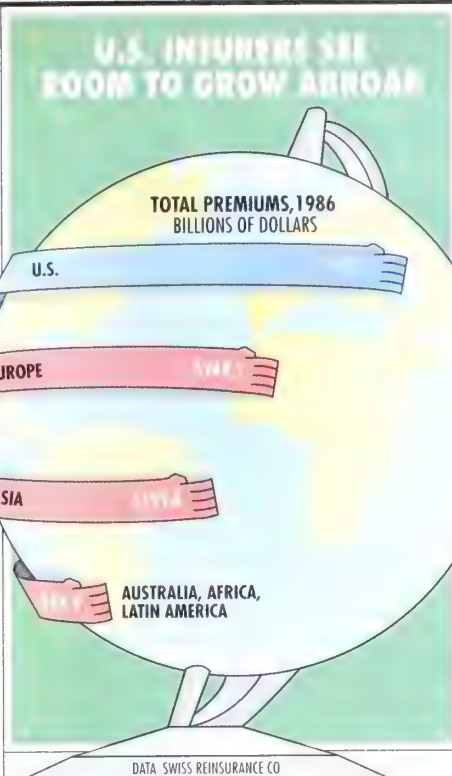
Margins in the U.S.
are so low, 'you're not
sure whether making
more sales is a good idea'

sing six separate computer centers with no central cash control and no corporate identity. ITT Corp.'s World Insurance Group, which draws its \$1 billion in yearly international premiums from Britain and Holland, formed a new subsidiary in Belgium and the rest of the EC.

Not everyone believes that even a 1992 Europe will be a pushover. "It is a bit of a stampede," admits H. H. Jenrette, chairman of Equitable Life Assurance Society. Nor is a Life & Casualty Co. starry-eyed over Europe. True, Aetna enjoys 10% annual growth in its Spanish business, and its other European operations are profitable. Aetna sees juicier profit and investment opportunities in the Pacific countries. Says John W. Rosensteel, vice-president of Aetna International Inc.: "1992 represents more of a globalization of the market than potential for great growth. That's far different from the scenario in the Far East."

THE LODGE. Companies are lined up to do business in the highly protected rich—Taiwan market. South Korea, despite its recent welcome to a number of American insurers, has plenty of interest in applying for permission to do business there. While waiting on government bureaucrats, many U.S. insurers have turned to Hong Kong's wide-open market. Aetna opened a regional office in Hong Kong in 1987. One lucrative business for Aetna is moving Hong Kong residents into dollar-denominated insurance policies for those eager to diversify their portfolios. The insurer also bought a 49% stake in a Hong Kong health insurance company and a 49% stake in a Japanese insurer. Aetna also hopes its Japan-based investment management subsidiary will expand into life insurance and individual pensions.

But it's Japan that U.S. insurance companies view as the mother lode. Although Japanese consumers carry more life insurance than Americans, the Japa-



nese penchant for savings is legendary, and the economy keeps growing. A recent analysis commissioned by Equitable projects a doubling of the Japanese life market by 1995. A number of U.S. insurance companies have already enjoyed success selling their pension-fund and money-management expertise to cash-flush Japanese institutions. And these same companies are pushing to sell more life insurance.

An all-star roster of American companies have set up shop in Japan. But the only success story thus far has been Georgia-based American Family Life Insurance Co., which landed \$1.4 billion in premium income in Japan last year from life policies that pay off only if the holder dies of cancer.

For more conventional policies, it won't be easy getting business away from Japanese insurance companies,

which are the biggest in the world. And the industry is tightly controlled by a Finance Ministry that doesn't thrill to talk of price or product competition. That means the company with the best marketing gets the most sales.

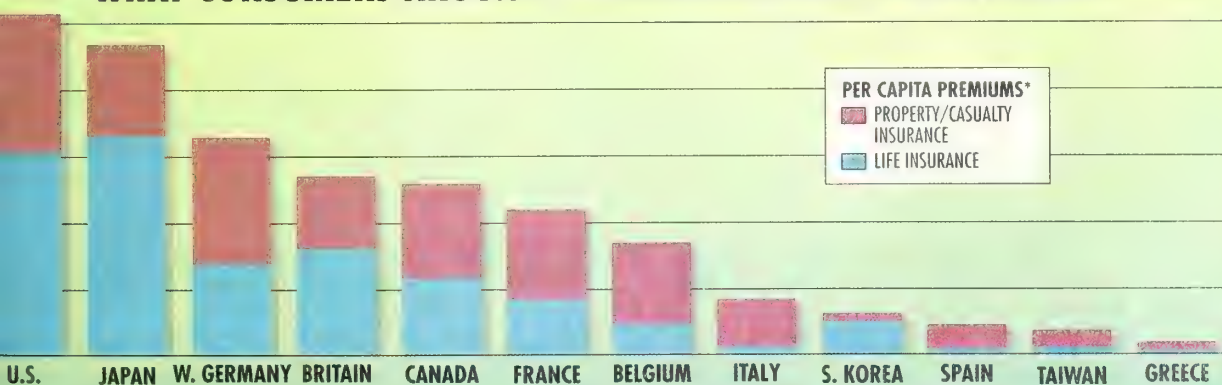
BROADER MIX. Equitable's marketing gambit is to sell only investment-oriented life insurance products to upscale Japanese. The insurer is emphasizing its competitive niche by hiring mostly college-educated salesmen. Equitable, which is building a 450-strong sales force, expects it will be at least 85% men. By contrast, most Japanese life insurers rely on women to sell their products. Nippon Life Insurance Co.'s 69,000-person sales force, for instance, is about 90% women.

Prudential, America's largest insurance company, wants to sell a much broader mix of financial products in Japan than Equitable. It doesn't plan on hiring women. "Our approach was to develop a very sophisticated financial-planner type sales force—only career-oriented males," says Kiyofumi Sakaguchi, president of Prudential's Japanese subsidiary. U.S.-educated, and the first Japanese fellow of the American Society of Actuaries, Sakaguchi has ambitious plans. "We're shooting for three or four times the productivity of typical Japanese sales persons."

Although their belated forays abroad could prove no less stressful than those of the banks and brokers before them, the U.S. insurers have little choice but to try. The insurance world of the future looks to be dominated by a few multinational giants offering a broad range of insurance products in all countries. And there aren't enough lucrative niches to go around for the rest. By investing heavily overseas now, American insurers are, in effect, buying insurance on their own futures.

By Resa W. King in Hartford, with Larry Armstrong in Tokyo, Steven J. Dryden in Washington, Jonathan Kapstein in Brussels, and bureau reports

WHAT CONSUMERS AROUND THE WORLD SPEND ON INSURANCE



DEAN WITTER BRACES FOR A BACKLASH IN BOSTON

An employee's arrest points to an office already under a cloud

For years, Walter F. Curran played the high-flying stockbroker. He pulled down commissions of up to \$170,000 a year from his employer, Dean Witter Reynolds Inc. Smooth and charming, he entertained prospects regularly at the local country club. He picked up dinner checks and drove the streets of Boston in a green Jaguar.

In fact, Curran was doing too well. This month his world came apart, creating a public scandal for Dean Witter's already troubled Boston office. Three weeks ago, Curran disappeared after taking about \$3.4 million of his clients' money. He didn't resurface until Feb. 17, when customs agents caught him driving a rented car across the Canadian border to Massena, N. Y. He had \$132,000 on him when he was arrested, authorities say.

TOO ASHAMED? The U. S. Attorney in Boston says Curran will be charged with bank and mail fraud. Since 1982, the government charges, he took \$2.6 million in cash from four investors—some of whom were his clients at Dean Witter—promising extraordinarily high returns. He said that he was investing the money in his personal account at Dean Witter, but never did. To keep them happy, he prepared false monthly statements showing how well they were doing, the government says.

Dean Witter officials think that many more investors were fleeced by Curran but are too ashamed to step forward. Curran allegedly used his customers' money to finance a lavish lifestyle—and then fled when his debts grew too large, say sources close to the investigation.

While that kind of corruption arguably could happen anywhere, few in Boston's tightly knit investment community were shocked that it occurred at the local Dean Witter branch. The firm sees no big problems: "I don't think that place is out of control at all," says Dean Witter spokesman James M. Flynn. But in the past year there have been complaints that the highly profitable branch was giving some customers a raw deal.

The Massachusetts Securities Div.

says it has been investigating Dean Witter's office for at least six months, since allegations arose that brokers there had "churned" some customer accounts to generate higher commissions and improperly invested some client funds in risky stock index options.

Two Dean Witter executives, including office manager Stephen J. Lozen, quit in the face of that investigation. But



■ THE GOVERNMENT ALLEGES THAT WALTER CURRAN BILKED INVESTORS OF \$2.6 MILLION AFTER PROMISING EXTRAORDINARILY HIGH RETURNS

even before that, the office found itself entangled in controversy. Juliette Wang Coombs, daughter of computer magnate An Wang, sued Dean Witter and a broker for losing \$2 million of her money.

State regulators say the Curran episode provides further evidence that Dean Witter's Boston office may be out of control. "We're concerned any time we see a pattern that demonstrates a

lack of supervision in any brokerage house," says Martin T. Meehan, deputy secretary of state for securities. He adds that his office's probe may eventually force Massachusetts to revoke Dean Witter's license to operate in the state.

It's more likely that Dean Witter, owned by Sears, Roebuck & Co., will move first to correct the problem. The firm denies any connection with Curran's off-the-books deals. But private executives worry that the office may have grown too large to control effectively. Its 100-plus brokers have already produced more than \$3 million in commissions so far this year, more than at other Dean Witter retail offices. For problems such as those of the past months, says one Dean Witter executive, "an argument against a brokerage having such a large office. We have much trouble supervising them that we prefer to keep them small."

Size is a concern for other firms, too. "To expect one branch manager to enforce the activities of 100 salesmen is expecting a lot," says Herold D. Gottmann, senior executive vice president at Shearson Lehman Hutton Inc. Most of the big firms, including Dean Witter, impose strict controls on their branches, requiring daily financial reports and regular audits.

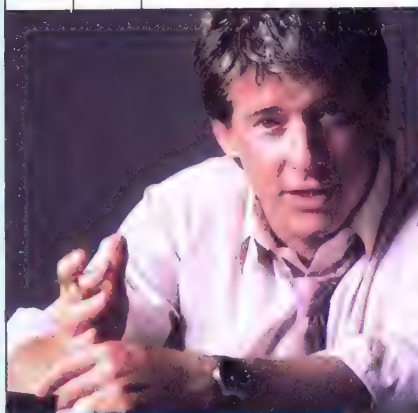
Dean Witter started making changes last year. In November it installed Edward M. Sullivan to replace Lozen. Sullivan had headed branches in Burlington, Vt., and Garden City, N. Y., and is respected within Dean Witter.

'BLACK CLOUD.' But the public scandal surrounding Curran's arrest has created new morale problems: On Feb. 16, Dean Witter President James F. Higgins and two other top executives visited Boston to calm brokers worried that the scandal would scare off new customers. The firm is mulling many strategies to boost its image in an important market. "Our image is under a black cloud," says one executive.

Dean Witter is planning to increase its donations to Boston charities, as well as its advertising budget, to polish its reputation. But the firm says it won't compensate investors bilked by Curran. Local competitors, not surprisingly, say retail customers will shun Dean Witter brokers for many years. But they fear, too, that Curran's allegedly illegal deals will undermine the public's confidence in brokers. Restoring that, they say, could take a long time.

By Keith H. Hammonds in Boston, and Jon Friedman in New York

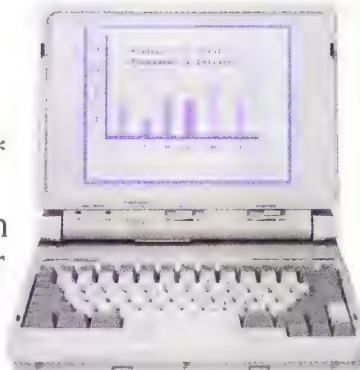
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THE GREATEST INVENTION SINCE . . . BURNT TOAST?

Investors say Shearson's unbundled stock unit is no bargain

Two executives at Shearson Lehman Hutton Inc., the Unbundled Stock Units (USU) looked like a godsend. Its Dec. 5 debut seemed to take Shearson off the hook for bungling the fight for control of RJR Nabisco Inc. When splashy headlines trumpeted the new investment product, Shearson brass was ecstatic. "The USU scored an immediate victory," gloated an official at the firm, "because it took our RJR defeat off the front page."

But the USU may well turn into another embarrassment. Investment managers are blasting the product, and Shearson has had to bring in Goldman, Sachs & Co. to help pitch the idea to institutions. "This has been a more difficult sell than Shearson ever thought it would be," says Terry A. Hamacher, managing director of Prudential Equity Management Associates.

Shearson insists that the unbundling concept is sound. USUs are based on the idea that investors purchase stock for essentially three reasons: current dividends, dividend growth, and capital appreciation of the shares. The firm says it signed up four blue-chip companies—parent American Express, Dow Chemical, Pfizer, and Sara Lee—to participate in the program. The companies would swap \$5.6 billion of their stock currently held by institutions for a bundle of three securities: a bond that matures in 30 years, a preferred share, which pays a dividend equal to future growth in the common stock's dividend, and an equity-appreciation certificate, which gives the owner the right to exchange it for a common share.

TOO CONFUSING? The allure for the public, says Shearson, is that the unbundled shares reflect varying investor goals more accurately. And some experts argue that the total value of the three securities would actually exceed that of the common stock. The appeal for issuing corporations is that unbundling reduces corporate taxes. The company substitutes interest payments, which are tax-deductible, for dividends.

But investment managers who are being asked to exchange their common stock for USUs are balking. Many think the product is too confusing, takes away

their voting power, and could in fact sell in total for less than the original security, depending on how liquid the markets are. Says Gary P. Brinson, president of First Chicago Investment Advisors: "This is a very regrettable idea. What's better about it?" George Reagan, equity manager of the Teacher Retirement System of Texas, agrees: "If there is any advantage to the investor, it is not discernible."

'This has been a more difficult sell than Shearson ever thought it would be.'

TERRY A. HAMACHER

Managing Director, Prudential Equity Management Associates

Shearson thinks the criticism is premature. "When you're going to turn the world upside down," says Ronald L. Gallatin, a Shearson managing director, "you can't do it quickly." In December, Shearson sent 30 analysts and investment bankers on the road to pitch USUs to 225 U.S. institutions, with still more meetings scheduled for March.

And on Feb. 8, in a rare move, Shearson distributed a report on Johnson & Johnson, not now a participating company, that attempted to show how much higher J&J's stock would be if it joined Shearson's USU group. "This is the most intensive effort there has ever been on the Street to launch a new business," Gallatin says. The firm still expects to have unbundled shares trading on the stock exchanges in April.

Shearson didn't foresee the big back-

lash from shareholder groups. The United Shareholders Assn., which was created by corporate raider Boone Pickens Jr., and Institutional Shareholder Services, led by Bob McCall, a former Labor Dept. official, both say the USU is "coercive" because investors must give up voting rights. The Securities & Exchange Commission, which voiced concerns about the loss of shareholder rights in USUs, will soon vote on whether they should be listed on stock exchanges.

HELPING HAND. Given Shearson's problems, it isn't surprising that the firm sent out an SOS to venerable Goldman Sachs last month. With the hope that Goldman could attract more institutional interest in USUs, Shearson agreed to give Goldman some of the expected \$10 million in USU fees that the issuing companies will be paying. Investors on Wall Street leaders read the move

as a weakness. Says a rival brokerage executive: "Do you think Shearson would have share fees with Goldman if it was having big trouble?"

Shearson is already considering proving the USU. It may attach voting rights, offer an additional 1% of dividend, or offer an additional 1% of unbundled unit for every share of common being exchanged, give a higher interest rate for the bond portion, or sweeten the dividend on the preferred stock.

Although investors don't love the move, they give Shearson credit for taking a chance. Says Prudential's Hamacher: "I'd give Shearson an A for effort and an A for creativity." Still, if USUs start getting a better reception, they could be headed for an F.

By Jon Friedman in New York, with bureau reports

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HOW A REAL ESTATE HIGHFLIER FLAMED OUT

A mortgage security proved too hot for Residential to handle

It could be a record: from a \$68.6 million initial public offering to belly-up in just six months. Some sleazy penny-stock deal? Not exactly. Residential Resources Mortgage Investments Corp., a Phoenix real estate investment trust (REIT), appeared to have all the right credentials. Donaldson, Lufkin & Jenrette Securities Corp. led a group of respected regional brokers that last June underwrote the offering, and some of Wall Street's biggest names, including Thomson McKinnon, Merrill Lynch, Prudential-Bache Securities, and Salo-

rectors. "Nobody ever dreamt they could be wiped out." A DLJ spokesperson said the firm "made all the disclosures that were appropriate." Attorneys for Residential declined comment.

But investors could very well be wiped out if the lenders to Residential prevail in a Phoenix bankruptcy court. Thomson, Merrill, Prudential, and Salomon often lent the REIT up to 95% of the price of the residuals they sold it. As collateral for \$200 million of loans, they hold the residuals that they now want court permission to liquidate. The four firms

generous yields but produce an erratic flow of cash. As homeowners "prepay" their loans, perhaps when they move or refinance, investors holding Ginnie Maes backed by those loans get back the principal in unpredictable chunks. In CMO, the Ginnie Maes are pooled to back bonds designed to return principal at more regular intervals.

When the CMO market took off in 1983—there are now \$200 billion of the outstanding—investment bankers began to pay dirt: They could buy Ginnie Maes for, say, \$200 million, pool them in a trust, and use them to back 30-year CMO bonds. Then they would find pension funds, thrifts, and mutual funds willing to pay, say, \$203 million for the extra convenience of CMOs. The \$3 million wasn't the only gravy for the bankers. After passing along the Ginnie Mae interest due to CMO bondholders, they typically had some interest left over—a "residual" cash flow of, say, \$50,000 every six months. They could either keep it or sell it to others like Residential.

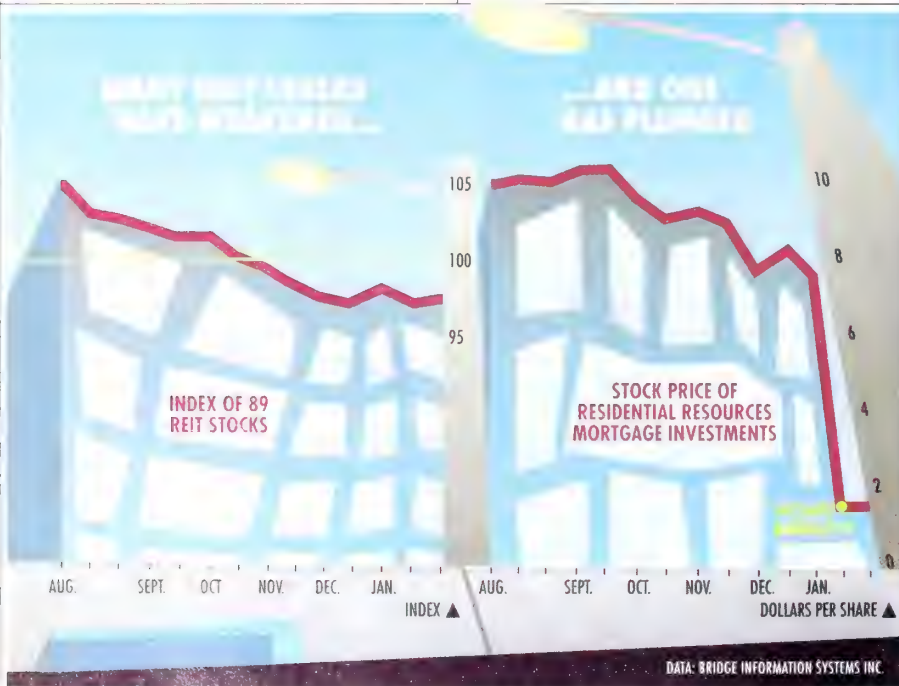
But as competition heated up, profit margins were squeezed. This sowed the seeds of the Residential fiasco. Suddenly the whole CMO business was "being driven by the residuals," says one investment banker. "Unless you could sell the residuals, you couldn't do the deals."

By 1988, traders daunted by the complexity of residuals were calling them the "toxic waste" of the mortgage business. Newfangled CMO bonds had adjustable rates. That meant that higher rates paid to bondholders left less cash for those—like Residential—who had bought the rights to the residuals. The 1988 surge in short-term rates afflicted REITs generally (chart), but none as severely as Residential.

MARGIN CALL. While a few other REITs also went into residuals, they didn't rely on doing so with Marshall's awesome leverage. Several brokers did try to get him away, but enough others were eager to keep the CMO mill churning. In September his original \$68.6 million equity controlled \$790 million in residuals. When rates ticked up in December and pushed down the market price of the residuals, Merrill made a margin call Residential couldn't meet. On Jan. 10, Residential filed for reorganization under Chapter 11 of the Bankruptcy Code.

Marshall and his underwriters had put what may be the most complicated securities yet into the hands of retail investors. And they did it in a way that left scant margin for error. Marshall, says a former colleague, "isn't a 'details' person. His ideas flowed faster than the follow-up." Which, sometimes, can lead to a long, slow day in court.

By David Zigas in New York



mon Brothers, lent Residential money.

Most REITs are a sort of mutual fund, holding such visible assets as shopping centers and office buildings, or the mortgages on them. Residential's investments, however, are in the far more nebulous "residuals"—arcane, volatile byproducts of complex mortgage financings, that could become almost worthless if interest rates surged. The individuals who bought the REIT were "in way over their heads," says Daniel Krasner, a New York attorney representing shareholders who are mounting a class action against DLJ and Residential's di-

aren't named in investors' lawsuits.

When James C. Marshall, Residential founder and former chairman, first came calling, the firms were honored to have him as a customer. As a partner in the Los Angeles-based accounting firm Kenneth Leventhal & Co., Marshall had helped transform lumpy bundles of mortgages into precise instruments that now rival Treasury securities in popularity. He declined to be interviewed.

The basic innovation was the collateralized mortgage obligation. The CMO fixed a flaw in traditional mortgage securities such as Ginnie Maes, which have



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BY GENE G. MARCIAL

PHELPS DODGE'S TREASURES MAY LIE BELOW THE COPPER

Many stock-pickers use Phelps Dodge as a copper play, since its stock invariably moves with the metal. But the smart-money pros now see Phelps also as an asset-rich, cash-laden company worth nearly twice its current price of \$56 a share.

When copper started its slide on Jan. 26, from \$1.62 a pound to \$1.31 in mid-February, Phelps reacted like a true copper stock, slumping from a high of more than 60 in late January to 54 on Feb. 15. The stock now has bounced back up to 56, thanks partly to aggressive buying by some money-movers.

These big investors contend that Phelps's management is aware that the company is vulnerable to a raid, and that it might have to undertake a large-scale asset restructuring. Right now there are no raiders holding big chunks of Phelps stock. But a few investor groups have been loading up, including Forstmann Leff Associates, which has an 8.6% stake, and Gintel Equity Management, with about 4%.

To stave off a raid, investors are betting that Phelps may eventually spin off 20% to 25% of its copper operations. The company may also part with some of its nonmining businesses, which account for 45% of total revenues of \$2.3 billion and about \$4 a share in net income. Last year, earnings on fully diluted shares were \$11.20 apiece. Estimates for 1989 range from \$12 to \$14 a share.

AMPLE EVIDENCE. Joseph Werner, vice-president of A. R. Schmeidler, a New York investment company that has been buying, values the copper operations alone at \$77 a share. He figures the industrial businesses are worth \$27 a share, for an estimated breakup value of \$104 a share. The industrial operations include Columbian Chemicals, the second-largest worldwide producer of carbon black, which is used largely in the rubber and printing industries. Then there's Accuride, the largest domestic maker of steel wheels and rims for medium-size and heavy trucks.

Management's other option is to take the company private through a leveraged buyout—at \$80 to \$100 a share. "There is ample evidence that the smart people who know the industry well have been willing to pay hefty

PHELPS DODGE: PERKING UP



prices to get hold of mineral assets," notes Ernie Mysogland, Gintel's chief investment officer. As an "efficient, well-managed, and low-cost copper producer," he says, Phelps is "one of the most undervalued and overlooked companies around." Management and the board, led by Chairman G. Robert Durham, own about 1% of the stock.

A FLOOD OF CHIPS FROM CYPRESS

The Street's skepticism toward technology stocks has been an unending trauma for high-tech companies and investors. Even Cypress Semiconductor, a highly publicized, small-capitalization growth company, is being jettisoned from analysts' buy lists. They fear that Cypress has already jumped too high, from 8 in early December to more than 12 in early February. But the stock hasn't collapsed—it's still trading at about 11.

One reason, says Michael Murphy, editor and publisher of *California Technology Stock Letter*, is that the company's new high-speed chips designed for high-performance personal computers "look as if they'll be winners and dominate the market." He is impressed by Cypress' growth prospects as a supplier of high-speed specialty semiconductors used mainly by computer makers, telecommunications equipment makers, and defense agencies for military applications.

Part of Cypress' strength is due to the speed at which it has been introducing new products—23 in the fourth quarter of 1988 alone, notes Murphy. He figures the company's sales and

earnings can grow about 50% a year even if a recession hits. Based on the rapid growth, the stock could reach this year, says Murphy. Earnings 1988 jumped 55%, to \$20.8 million, 56¢ a share, and revenues climbed 80% to \$139 million. This year, earnings are expected to rise to 75¢ and revenues \$200 million. Murphy also notes that Cypress has about \$89 million in cash or about \$2.50 a share, and is debt-free. The company has been using part of that cash to buy several innovative young semiconductor firms to maintain its competitive edge.

ARE RAIDERS RIGHT BEHIND RITE AID?

Analysts were surprised in early December when Rite Aid announced that third-quarter results would be way below the year earlier net of 49¢ a share. The stock promptly dropped from 35 to 29. But now it's back to nearly 35, thanks partly to the company's upbeat estimate that earnings for fiscal 1989, which ends on Feb. 28, should be modestly higher than last year's, despite the third-quarter setback. But that's not the main reason the stock has been rising again, say some arbitrageurs and investors. The more potent factor—you guessed it—takeover talk.

Fueling the whispers is the unusually heavy volume in recent weeks. Another intriguing giveaway that something may be afoot is the aggressive buying lately by Bear Stearns. The New York securities firm, which is said to have bought some 6 million shares, is believed to be buying on behalf of a big client. Bear Stearns Chairman Al Greenberg declined comment.

One investment manager who is buying the stock puts Rite Aid's estimated breakup value at \$50 a share. The company, which operates more than 2,100 discount drug and beauty-aid stores located mainly in the Northeast and Southeast, also operates 74 auto-parts stores, 46 discount bookstores, and 10 dry-cleaning establishments.

Rite Aid certainly looks right as a takeover bet, says one pro. But he warns that profit margins over the short term may remain under pressure in part because of continuing store renovations and slowed sales at the auto-parts unit. Without a takeover, the stock is definitely overvalued, he contends. But right now, takeover is the game. And a management LBO isn't out of the question either, he says.

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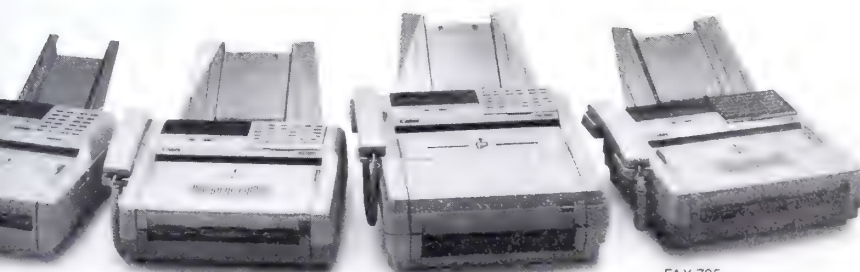
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5, Jean Luc Grand-Clement saw handwriting on the wall for the semiconductor industry: There would be more and more chip designs, but fewer of each would be needed. He quit his job as head of Motorola's European chipmaking operations and founded a company called European Structures (ES2). Its mission was to offer new ways of designing and making custom chips—in tiny volumes. He predicted that demand for this would propel sales to \$100 million in just five years.

Grand-Clement admits the timetable has slipped, but only by seven years. He expects 1989 sales to be more than last year's \$13 million. The \$100 million now projected is for 1991. Even today, the yearly number of new designs put into production is 25 in 1986, 107 in 1987, and 310 in 1988. This year, more than 700 new designs are expected.

Europe's chip using is moving to ES2, Grand-Clement figured it was time for the acid test: the U.S. market. So in February, ES2 formalized a partnership with United Silicon Structures (US2) to prove that catering to small-time orders will pay off among the hot business opportunities of the 1990s.

CALL. "Ultimately, there's got to be a restructuring of the semiconductor industry," says US2 Chairman Henri Jarret. "Service-oriented engineering companies must emerge. When a customer wants 10 units of this or 20 units of that, there is nobody in a position to provide that level of service."

He should know. He used to be chief of VLSI Technology Inc., a \$125 million specialist in so-called application-specific integrated circuits, or ASICs. That was a compromise way of putting proprietary technology on silicon by combining elements of standard chips,

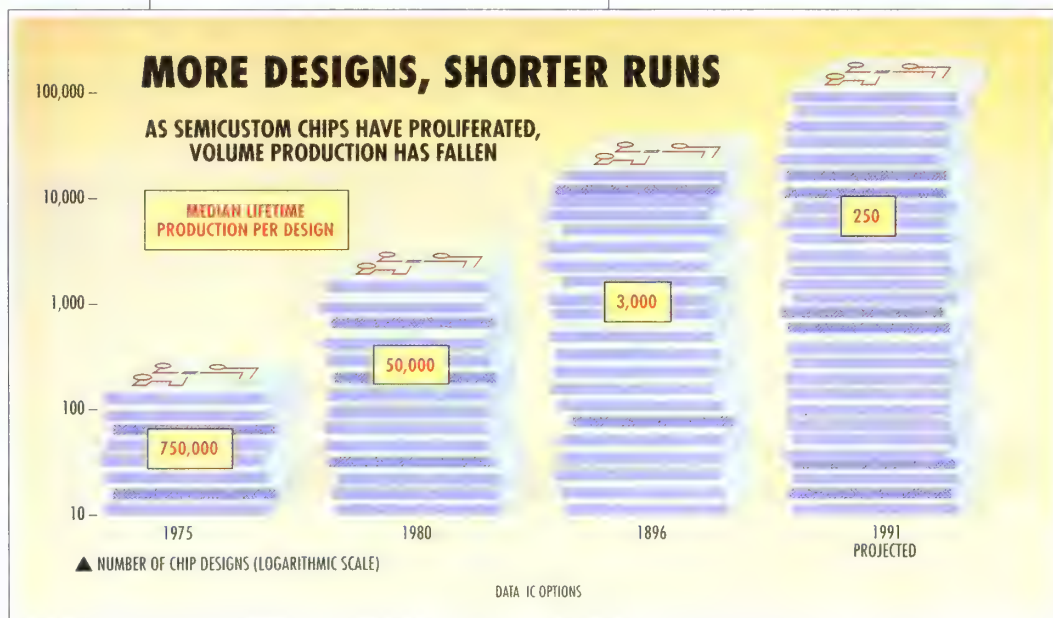
which can be had for a few dollars, with some measure of custom circuitry. This "hard-wired" approach can protect the inner workings of electronic systems better than software, which is easier to copy. It also avoids the usual million-dollar price tag of a "full-custom" IC.

But US2, based in Palo Alto, Calif., plans to bypass such compromises. The spinoff will produce fully customized designs in short runs and deliver them in a month—at bargain-basement prices. That will allow the company to tap into

neers are already generating close to 600,000 new designs for printed-circuit boards annually, and the number is climbing by about 10% a year. That adds up to mammoth market for ASICs. "Five or 10 years from now," notes Jarret, "if the industry is producing 1 million boards per year, and there is just one ASIC for every board, we would have at least 1 million IC designs per year." Today, he adds, less than 5% of all circuit boards contain even a single ASIC.

BIG APPETITES. Those figures persuaded some venture capitalists to ante up seed money. For a 30% stake, Boston's Advent International, which had been ES2's leading backer, Dillon Read/Concord Partners, and Mohr-Davidow Ventures chipped in a total of \$4.7 million. An additional 30% interest is reserved for US2's key employees, and ES2 is keeping the remaining 40%.

Because the U.S. chip market is six times Europe's and gobbles up 250% more semicustom designs, "US2 could



the exploding demand for small-volume customized circuits. Projecting current trends out five years points to a mind-boggling market of 700,000 to 1 million new designs annually.

Even Jarret was skeptical of those numbers. So he did some checking. True, there is no way the world's 10,000 chip designers could generate that many designs. But the electronics sector as a whole employs more than 300,000 systems engineers. If the population of electrical engineers remained static, which it won't, each engineer would need to create only three designs per year.

Given the growing sophistication of automated-design tools, that seems feasible—especially since systems engi-

neers are much bigger than ES2," notes Douglas R. Brown, senior vice-president of Advent International and a US2 director. "I'm very enthusiastic," says William H. Davidow, a former senior executive at Intel Corp. who moved into venture capital as a partner in Mohr-Davidow.

In general, US2 will replicate what ES2 is doing in Europe: dispensing not only with the usual stable of standard ICs but also with such halfway measures as gate arrays. These chips are mass-produced as featureless grids of transistors, then reprocessed in small batches to connect the transistors and create ASICs with different "personalities."

Instead, ES2 worked with Britain's Lattice Logic Ltd. on computer-based

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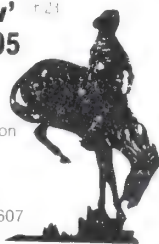
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techniques that enable a customer to fabricate its own chips from scratch. Intel's contribution was a so-called logic compiler, a computer that takes a list of functional specifications and converts them into a circuit design. silicon compilers, now installed at 2 design centers sprinkled around Europe even engineers who have never before tackled an integrated circuit design can come up with a winner. Says ES2 President Jean-Pierre Demange: "We've got a very high success rate with people designing chips for the first time."

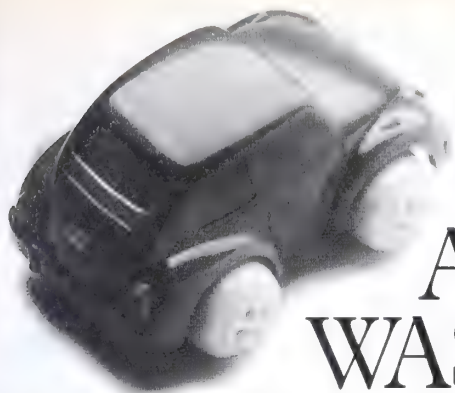
Duplicating that success here is a challenge. If US2 has to provide more token engineering support, design costs will stretch and costs will soar. A typical client spends about four years and \$28,000 for a full-custom design of prototypes. Jarret expects to hold design costs to \$15,000 and deliver in as little as two weeks on a rush order.

Once a design is complete, US2 turns to another strategic weapon, a million electron-beam machine. ES2 has two of these systems, which shoot out needle-thin beams of electrons under precise computer control, etching circuits directly onto a silicon wafer by tiny line. Other chipmakers use E-beams to make the "negatives" which chips are printed in volume. Until recently the process was too slow to consider for "direct-write" production. Then Perkin-Elmer Corp. developed a system that processes 20 wafers an hour, each with up to four different designs. **'SCARED TO DEATH.'** US2 is off to a winning start. Last year its European client sold about \$1 million worth of chips to several large U.S. companies. Jarret knows that US2's success hinges on attracting hordes of smaller companies. And he admits that most of its potential clients "are scared to death" of designing their own chips. Computer-aided design systems are expensive and take too long to learn to use them. Horror stories abound about companies that had to redo faulty designs.

"Someone has to stand up and say, 'we will guarantee the silicon,'" says Jarret. "Someone has got to figure out a way to reduce the training from five weeks to four or five days." "Someone has got to say, 'no, it will cost \$100,000, it will be \$10,000 or \$15,000.'" He concedes that implementing this vision will be tough.

But ES2 seems to be working the rope. And if the idea takes off in the U.S., the concept's backers already have their sights trained on the next target: Japan. It will be called JS2, says Adv Brown—for Japan Silicon Structures.

*By Otis Port in New York, with
Peterson in Paris*



NOT LONG AGO, MICHIGAN WAS JUST A KID IN THE PLASTICS INDUSTRY.

The kid sure has come of age. Why, in the mid-1980's alone, Michigan accounted for half of all new plastics-related jobs in the Great Lakes States and one-quarter of the plastics job growth nationally. And not simply because of the increased use of plastics in the auto industry ■ Many industries draw on the expertise and resources of Michigan's growing number of plastics application centers. Fabricator support industries are already in place. Resin producers benefit from nearby chemical feedstocks. Then there's Michigan's state government: committed to providing the best possible climate for expansion and growth. ■ The right markets are here, too. As Carl Haas, President of Blue Water Plastics, puts it, "Michigan is a great environment for expansion. We could not service our customers if we were in Illinois or Tennessee. We need to be where the engineering centers are." ■ There are many other reasons to consider Michigan. Call (517) 373-8495 or simply write Doug Ross, Director, Michigan Department of Commerce, 525 W. Ottawa, Lansing, MI 48909

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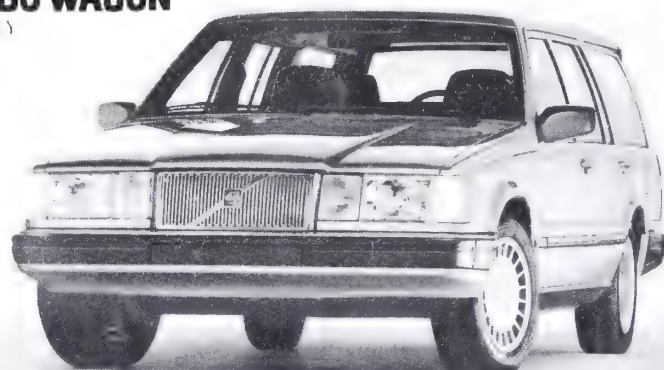


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Developments to Watch

BY WILLIAM D. MARBACH

ING BRAINY COMPUTERS OLDER HEADS



Computer scientists working with circuits that attempt to mimic the human brain have been reporting tantalizing progress. These so-called neural networks seem to possess some degree of innate intelligence. There's a problem, though: Neural net chips just won't be able to take the heat.

That's because neural are based on analog technology, not the digital language ones and zeros used by today's computers. Such microcircuitry is much more temperature-sensitive than digital transistors. That could affect reliability when neural nets move from lab to factories or other harsh environments.

Steven G. Morton, a former ITT Corp. researcher, formed Lord Computer in Oxford, Conn., to pioneer neural nets based on digital memory-chip technology. Although Morton's ideas were met with widespread skepticism, scientists at Massachusetts Institute of Technology recently scrutinized his claims and pronounced them apparently sound. The acid test comes in May, when Morton promises to have sample neural-net chips for evaluation by potential customers. Next, Morton plans to use the digital-net chips to build a prototype system, which he predicts will be phenomenally fast: capable of at least 16 billion operations per second.

S. BIOTECH IS BIGGER, JAPAN'S MAY BE BETTER

Does Japan have the lead in biotechnology? Not quite yet, says a recent study by the Food & Drug Administration.

U.S., in fact, has twice as many pharmaceuticals approved for marketing or in clinical testing as the Japanese.

Henry I. Miller, special assistant to FDA Commissioner Frank E. Young, compared the results of his survey of Japanese biotech companies with data from a study of U.S. companies conducted by the Pharmaceutical Manufacturers Assn. It showed that 24 Japanese companies had 42 products in clinical testing or beyond. But 54 U.S. companies had 97 products at the same stage.

The Japanese, however, have a wealth of potential products—143 reported in the survey—in the early testing or research phases. Some, says Miller, are “far out,” including using musk as an analgesic and cloning bone proteins to treat osteoporosis. “It’s surprising because you usually hear about Japanese licensing U.S. developments,” says Miller, “but they’re being very innovative.”

LL 'ER UP WITH -RAPESEED OIL?

Heinrich Hövelmann, mayor of Papenburg, West Germany, the smell of french fries doesn't mean lunchtime. His town runs on rapeseed oil, a vegetable oil used in cooking.

Hövelmann is taking part in a government-sponsored pilot project to start an environmentally friendly cycle: Farmers

would grow rape on their fallow fields, then bring their crop to an oil-extraction mill at a local recycling center. The center would produce oil to be used for auto and tractor fuel and fertilizer for the next crop. And the straw can be used for packing material.

So far the diesel car has run 8,700 miles without problems. Lothar Müller, a mechanical engineer who heads the project, claims that fewer exhaust fumes are emitted than from a normal engine, enabling it to meet Europe's emission standards but not the tougher U.S. benchmarks. In principle, he adds, every diesel motor could be reset to run on rapeseed oil.

INTEL'S NEW N-10: A SUPERCOMPUTER-ON-A-CHIP

Intel Corp. unveiled its new supermicroprocessor, code-named the N-10, at the mid-February International Solid-State Circuits Conference in New York. The chip handles 64-bit-long instructions, double the 32-bit length of Intel's current microchampion, the 386. It has three parallel processors, one of which features reduced instruction-set computing (RISC). As a result, the N-10 blazes along at a phenomenal 150 million operations per second and does scientific calculations faster than the processors in supercomputers from Cray Research Inc. “This is like putting a Cray on a chip,” boasts David L. House, head of Intel's microprocessor group.

House clearly believes the N-10 will outgun rival RISC chips. Not only is it much faster, but it also is the first chip that integrates vector processing, the basis of scientific computing. But he insists that the supercomputer-on-a-chip won't cannibalize Intel's coming 486 microprocessor, successor to the 386. The 486 will be so fast, in its own right, that even the N-10 can't touch it when running software compatible with the huge population of IBM-type personal computers. Instead, Intel says the N-10 will open new markets, from workstations to full-blown supercomputers. Look for the N-10's formal introduction in late February, when Intel may also unveil the 486.

AN ICY WAY TO GET TAILS WAGGING

If you own a dog, it may happen every time you sit down to eat a bowl of ice cream. Fido appears from nowhere, assumes his best “beg” position, and looks at you with those soulful brown eyes. In the back of your mind you know that ice cream is bad for the pooch, but he persuades you to let him lick the dish clean.



The problem is that older dogs have trouble digesting lactose, a protein found in dairy products, and the high sugar content in ice cream provides nothing but empty calories to your pet. Now, William J. Tyznik, a professor of animal nutrition at Ohio State University, has developed Frosty Paws, an icy treat for dogs. Made from whey, it contains no lactose and is also salt- and sugar-free.

Dogs like it anyway, says Tyznik, because the big appeal of ice cream in the canine world is really just its coldness. Frosty Paws is being produced by Associated Ice Cream of Westerville, Ohio, and will be distributed nationally through supermarkets. If you feed Frosty Paws to the kids by mistake, don't worry—it's safe for human consumption.

FILING A TAX RETURN THAT DOESN'T SET OFF ALARMS

Dear Taxpayer:

We selected your federal income tax return for the year(s) shown below to examine the items checked at the end of this letter. We have scheduled an appointment for you....

ed to select audit victims, goes one specious piece of advice. Other ideas fall into the gray area between reality and myth. Many taxpayers think that large refunds, amended returns, and requests for extensions all increase your chances of having to lug shoe boxes full of receipts and documents to the nearest IRS field office. Some believe that preparing your own tax return makes you more vulnerable, on the theory that you are more likely than a professional to make mathematical errors that will draw the attention of the IRS. (It's not hard to figure out who started that one.)

Yet some bits of audit folklore are based squarely on fact. Take a deduction for a home-office (an often abused bit of the tax code), and the IRS may at the very least look more carefully at your return. Admit to a Swiss bank account or a brokerage account in say, the Cayman Islands, and an IRS agent may start asking all sorts of nasty questions.

The sad fact is, no one really knows for sure what criteria the IRS uses to decide who gets audited. Its computer model, the Discriminate Function System, picks out returns that don't conform to normal patterns of income and deduction levels. But the agency isn't telling what those patterns are—or which items it weighs most heavily in its calculations. And in case anyone does catch on, the IRS modifies the program every few years.

In that atmosphere of relative ignorance, audit-phobic taxpayers will do strange things to dodge a bullet from the IRS. According to Jerry Willaford, a certified public accountant with Grant Thornton in Houston, one prominent client insisted on sending the IRS a check every year even if he was entitled to a refund (so far, so good). Yet, says Willaford, "we've had clients with refunds of over \$100,000 who have never been audited."

A wealthy client of one Big Eight accounting firm, although he lived in New Orleans, insisted on having his returns prepared in Chicago every year. The reason: Returns filed in some regions are less apt to be audited. The latest IRS data shows that 2.5% of 1986 Nevada returns were examined, against only 0.5% of Rhode Island's. The chances of IRS scrutiny are almost equal, it turns out, in New Orleans and Chicago.

Tax experts say there were strategies that used to be effective, but the IRS has since caught on. Filing late in the tax season was one: The agency used to pick most of its audits from among earlier filers, says Marvin Michelman, a senior tax manager at Deloitte Haskins & Sells. Another

other play was an outrageous deduction for charitable contributions. "The IRS's theory was that a person giving of his income might be a saint, but someone giving 50% of income to the Church of Perpetual Deduction probably wasn't," says Michelman. He adds, however, that the IRS



PREPARING YOUR RETURN INSTEAD OF HAVING A PRO DO IT MAY NOT MAKE YOU MORE VULNERABLE

Few form letters are more chilling than an audit notice, and this year the Internal Revenue Service is sending out about 1 million of them. In the \$50,000-plus income group, you stand about a 2.5% chance of being on the receiving end. And in the course of 20-odd years of filing, you have at least a 50% chance of being audited.

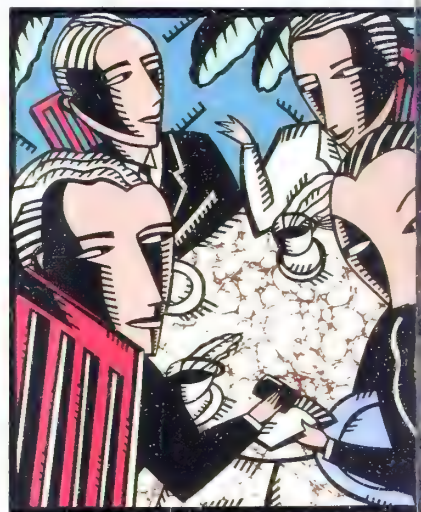
In the quest for some way to beat the odds, taxpayers and their accountants have long tried to figure out what triggers an audit—and strategies for avoiding one. Some notions border on superstition: Don't use the address sticker provided by the IRS on your return, because it's cod-

ed to select audit victims, goes one specious piece of advice. Other ideas fall into the gray area between reality and myth. Many taxpayers think that large refunds, amended returns, and requests for extensions all increase your chances of having to lug shoe boxes full of receipts and documents to the nearest IRS field office. Some believe that preparing your own tax return makes you more vulnerable, on the theory that you are more likely than a professional to make mathematical errors that will draw the attention of the IRS. (It's not hard to figure out who started that one.)

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WHAT'S BUSINESS, WHAT'S PLEASURE IS IN THE EYE OF THE BEHOLDER. IF THAT EYE IS THE IRS,

longer falls for that.

Yet many tax accountants and former IRS auditors agree that certain items are more likely to be flagged than others. Perennial favorites include deductions that are difficult to prove—such as employee business expenses, noncash donations, and casualty losses.

CONSISTENCY COUNTS. Another source of trouble is the IRS's Document Matching Program, which compares information on your return with information on W-2s, 1099 forms from your employer, brokerage house, banks. Here, you are more likely to be questioned about innocent omissions and

s made in recording income. Usually such an over-estimate will only trigger a letter from the IRS informing you of a deficiency. But sometimes the errors spark broader examinations.

Be careful to report your income under the name listed by your bank or broker. For example, you may be reporting dividends to the company whose stock you own while the IRS is listing them under the name of your brokerage house. When the computer fails to pick up the name of your brokerage on your return, it will send a warning signal to the auditor. Although you may be able to explain the glitch in time, the IRS agent

without those expenses," cautions Willaford.

■ **Charitable contributions.** Since putting a value on many types of noncash items donated for charity can be a subjective process, examiners often question deductions in this area. The Salvation Army, a popular channel for noncash contributions, publishes a free booklet of guidelines for valuing your donations. Also, the IRS might come calling if your total contributions amount to more than 15% of income.

■ **Casualty losses.** These send up an alert because many taxpayers don't understand the tax law in this area. First, it is difficult to prove that an item that is gone was actually stolen. Also, many think they may deduct the fair market value, when they may deduct only the cost. That means you are out of luck if someone steals a diamond ring that was a gift. "Many times we advise clients not to put the deduction on the return if the loss is small," says Willaford.

■ **Schedule C filers.** Many who file this schedule (those who are self-employed but not incorporated)

used to believe that they were less likely to be audited than are incorporated entrepreneurs. But Gerald Portney, a former IRS district director now at Peat Marwick Main, says low compliance among this group has led to increased IRS examinations of these taxpayers.

■ **The alternative minimum tax.** This is a tax on tax deductions. While the new tax rates are lower, the AMT is designed to make sure that sophisticated taxpayers with numerous deductions pay at least a modicum of tax. Say you have many items on your return that are subject to the AMT—such as large charitable contributions, losses from passive

investments, and the exercise of stock options. If you seem to be paying little or no AMT, the IRS may take closer look at your calculations.

■ **Individual retirement accounts.** Under the new tax law, taxpayers covered by another retirement plan—either their own or their spouses'—cannot deduct contributions to IRAs. And those with incomes above certain levels cannot take the full write-off. The IRS may want to double-check to see if those who are taking the IRA deduction are involved in another pension plan.

■ **Passive income losses.** The new tax law has made it more difficult for taxpayers to shelter income by investing in ventures with large losses.

Now taxpayers may deduct losses from so-called passive investments—such as tax shelters and some rental properties—only from income generated by those ventures. Because the definition of what constitutes a passive investment is so complicated, the IRS may want to give your interpretation a once-over.

While there are many steps you can take to avoid an audit, there's nothing you can do if you are one of the 50,000 or so taxpayers randomly selected each year to participate in the Taxpayer Compliance Measurement Program. If you are called in for a TCMP audit, every item on your return is open to scrutiny and the IRS will obtain bank records and other evidence for cross-checking. There's one small consolation: The government is not empowered to bring criminal charges based on what a TCMP audit turns up.

Once you are called in for an audit for any reason, tax experts advise clients to remain calm when dealing with the IRS. You may be subjected

to only a correspondence audit, where you will be asked by mail to pay additional taxes on specific items. Or the IRS may call you—and your documents—in for a face-to-face "office audit."

Experts cite both pros and cons to hiring a tax expert to represent you in an office meeting. Mary Sprouse, a Los Angeles-based tax attorney and a former examiner for the IRS, believes that professionals will "antagonize an auditor almost from the moment they sit down." Because the tax expert is out to win his case, he is likely to be more abrasive and aggressive, Sprouse says.

Others caution against representing yourself. "I'm a



WORKING AT HOME IS A BRIGHT RED FLAG: YOU DEDUCT, YOU MAY TRIGGER AN AUDIT

might then make a closer inspection of other items on your return. Tax reform, of course, has made audit bait out of other formerly routine things, including deductions for individual retirement accounts, passive income, and the alternative minimum tax. Here are some tips for avoiding trouble:

■ **Travel & Entertainment Expenses.** Auditors zero in on these deductions because of the fuzzy lines distinguishing expenses for business and pleasure. With a small company, the IRS might take a closer look "if your T&E expenses are more than 5% of revenues" or if your unprofitable firm could have shown a profit



ANOTHER BIT OF LORE THAT'S TRIED AND TRUE: FOREIGN BANK ACCOUNTS ARE AUDIT BAIT

very big believer that clients harm themselves by being their own advocates," says Henry Ritter, a partner at Ernst & Whinney. For example, you may tip the examiner onto other mistakes just through small talk or plain nervousness. Whether you represent yourself or hire an expert, the best rule of thumb is to maintain a reasonable demeanor.

While the mysteries surrounding the audit abound, taxpayers need not be overly fearful. If you have made an honest effort to follow the tax laws and keep records to document the items on your return, you will have a good defense. *Catherine Yang*

Smart Money

IS IT TIME TO START PANNING FOR GOLD STOCKS?

Buy gold stocks when the price of gold bullion is falling. Sounds crazy, no? But there's a method in the madness. Although their performance usually reflects that of the metal, mining equities have rallied 9% since December, even as bullion has continued to slide.

While bargain-hunting has pushed up prices, the trend also reflects better industry fundamentals. Many North American companies have announced expansion plans that will enable them to become bigger and lower-cost producers. Unless the price of the metal declines drastically, the stocks offer good appreciation potential.

If you want to own gold equities outright, it's best to stick with North American producers, rather than more risky South African or Australian mines. After a 20% decline in 1988, many are now undervalued. By all means, avoid extremely speculative exploration outfits. "Only one out of 3,000 ever makes it," says Kenneth Gerbino, a Los Angeles investment manager. Instead, invest in either active producers—the industry's blue chips—or developmental companies with mines about to come on stream.

Among active producers, look for companies with an annual output of at least

100,000 ounces of gold, preferably from several properties. August Arace, co-manager of the Freedom Gold & Government Trust, recommends American Barrick, whose stock has surged from 16 to 20 since December on news that it is increasing production at its Goldstrike mine in Nevada. Another player in the rich Nevada region is Echo Bay, now 15, which has the added attraction of producing its gold at \$220 per ounce, vs. an industry average of \$259.

MAGIC PAN? Among developmental producers, there's Galactic Resources, a Canadian firm whose mines range from South Carolina to California and the Philippines. At 3, "it has so many possibilities that it will be profitable even if only a few pan out," says Jeffrey Nichols, president of American Precious Metals Advisors.

In the long run, bullion's course dictates the shares' performance. So most pros have been buying slowly, holding back "until we see a positive price action in gold," says Kevin MacLean of Toronto's Cavelti Capital Management. Still, because equities are twice as volatile as bullion, they're worth checking out now. If a rally occurs, you don't want to be the last one joining the gold-stock rush.

Troy Segal



EVEN MANY 20TH CENTURY COLLECTIBLES ARE RISING IN VALUE

Collecting

AN OLD QUILT CAN BE A MIGHTY COMFY INVESTMENT

Remember that old quilt you slept under as a child? It could be worth a fortune on today's antiques market. A 1916 quilt filled with cartoon characters that was called "Funny Papers" brought \$300 just 10 years ago. It was auctioned at Sotheby's a few months ago for \$18,700. And a 1937 floral quilt called "Center Medalion" tripled in value over the past five years and recently sold for \$20,000, according to the seller, Thomas Woodard of the American Antiques & Quilts gallery in New York.

While few have the high level of artistry to command such prices, many 20th century quilts are rising in value. Even such common designs as "Double Wedding Rings" and "Sunbonnet Sues" of the 1920s and 1930s are fetching \$500 or more at Woodard's shop and at America Hurrah Antiques, also in New York. There are "still thousands around that haven't come out of the chest," says Woodard.

Expect to pay at least \$500

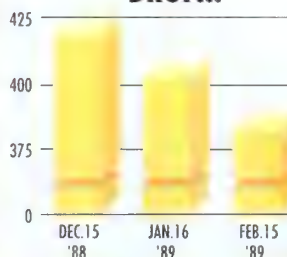
for a collectible quilt in a specialty shop; finer examples start at \$5,000. But you still pick up bargains at garage sales or by buying from the quilters themselves. Investors say 20th century quilts which are easy to spot because of bright pastel fabrics or whimsical subjects, are appreciating at about 10% year. As with any collectible, however, the appraised value is almost always higher than the eventual resale price.

What to look for? Naturally, quality and condition are key factors if the design is popular one. The quilt should have 8 to 12 stitches per inch, seams that are aligned, pleasing colors and fabrics.

With unique quilts, craftsmanship is less important. Indeed, a 1930 quilt depicting a black doctor caring for a white patient, sold for a few dollars in the 1960s. Despite the quilt's ordinary workmanship, a collector purchased last year for more than \$50,000.

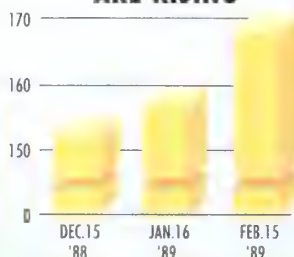
Sandra Atch

DESPITE BULLION'S DROP...



▲ DOLLARS PER OZ.

...GOLD STOCKS ARE RISING



▲ INDEX OF 26 NORTH AMERICAN COMPANIES

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The right choice.

To one camp of devoted anglers, battling the high-spirited bonefish in the Florida Keys' warm, shallow waters is what fishing is all about. But the bone, as it's known, remained relatively obscure until George Bush's pursuit of it in January.

Bonefishing is sedate compared with the high-seas adventure of going for marlin. And you usually throw the homely creature back after hauling it in—it's too bony to eat. But if you're still dying to know what the President sees in the sport, more than 40 outfits in the Keys offer guided expeditions through the grassy "back country" from Key Largo to Key West.

My pursuit of the bone started at Hawk's Cay Resort & Marina in Duck Key, Fla., 95 miles south of Miami. For \$185 I chartered an 18-foot, flat-bottomed boat captained by Matt Pribyl, one of many bonefishing guides in the Keys who know the vast flats intimately. Once in the foot-deep waters, the guide cuts off the motor and pushes the boat with a long pole to his favorite holes. He can also spot schools of bone under the water. And for the queasy, he will be the one who bites the head off the shrimp and baits your hook. Some anglers, however, prefer fly casting for bonefish with wet flies.

KEY FACTOR. While usually weighing no more than 10 pounds, the bone is powerful and wily. Skillful casting and boatmanship are crucial, since the fish spook easily. The real

Outdoors

THE UGLY, INEDIBLE FISH THAT HOOKED A PRESIDENT

fun begins once the fish strikes. Bones can bolt at 30 mph and usually take at least 20 minutes to land. I wasn't aware that I had a strike until I started reeling in my line for a periodic look-see. It jerked back—hard. After a half-minute of struggle, the 8-pound-test line snapped. My

waters, you are limited to a few shallow spots, you can't see the fish, and you can't cast with any accuracy. Good guides will cancel or postpone appointments if conditions aren't right.

When the weather is warm, as it has been this year, your guide should have no trouble

cluding bait and fishing tackle, for a maximum of two people. You can go out for a day for \$185. Guides can be booked at numerous hotels and marinas in the Keys. a good list, along with a down on fishing conditions, call World Wide Sportsman Islamorada (305 664-4615).

STONE-CRAB PIE. The best is to stay at a resort. Hawk's Cay offers a "Presidential Angler Package." It includes five nights at the lush oceanfront resort, two trips with guide to go for bonefish, tarpon, and one deep-sea

cursion for stone-crab game as marlin, sailfish. The cost is \$840 per person, plus occupancy.

If you want to trace the President's rubber-booted steps, check into Cheeca Lodge in Islamorada, 75 miles south of Miami. Bush didn't stay there (he stayed with friends), but the Secret Service and hordes of photographers did. He dined at the resort, which offers a "Presidential Angler" package of stone-crab pie, blue-crab, breaded grouper, and wine. It also has a \$900-a-day "Presidential suite" with a whirlpool in the kitchen.

The newly refurbished Cheeca, the Keys' premier fishing resort, also offers rooms and villas for \$199 to \$285 in season, which runs Dec. 23 to Apr. 1. After that, they drop to \$140 to \$190. Cheeca has meeting rooms, a nine-hole golf course, and its own boats for fishing and diving. *Pete Engle*



USING A PLATFORM TO HELP HIM SPOT BONEFISH, AN ANGLER FLY CASTS IN THE FLORIDA KEYS

guide guessed that I had kept my line too slack, giving the fish enough time to wrap it around a sponge.

It was my only strike of the day, but that was my fault. I insisted that we go out on a day that, although clear, happened to be quite windy. Weather is a key factor in bonefishing. The real sport entails spotting a school in the water, stalking it, and casting the bait a foot or so from their snouts. In choppy

finding bone. The elements were ideal on Jan. 13, when Bush landed a 13-pounder. "There were too many fish," says Bush's guide, George Hommell. "Schools were running into each other. He would cast, and they would explode all over the place."

A typical bonefishing trip costs about \$250 per day, in-

Worth Noting

■ **PENSION PLUSES.** IRS inflation indexing lets you put up to \$7,627 of pretax salary in a 401(k) plan in 1989, up from 1988's \$7,313 cap. And if you retire in 1989, the

most defined benefit programs can pay out (unless you're grandfathered) is \$98,064, up from \$94,023.

■ **NAME GAME.** Dallas' Salinon Corp. (214 692-9091) offers a free 16-page pamphlet on how to create a clever name for a new product or

company. Or for \$150, you can have its "Namer" software to run on your PC.

■ **SHINING SKIS.** For next winter, Volant is readying skis with sides and top fashioned from one piece of stainless steel. The Boulder (Colo.) company says that

the faster you go, the more stable you'll be. About \$3,000.

■ **MOBILE MESSAGES.** Rent an Avis car in England and Apr. 1, and you can request a free car phone. You'll get an answering-service number to check for messages from callers anywhere.



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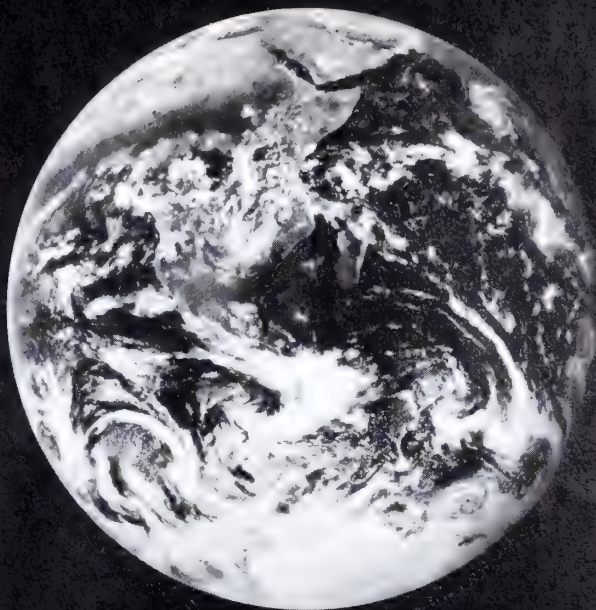
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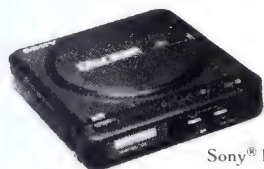
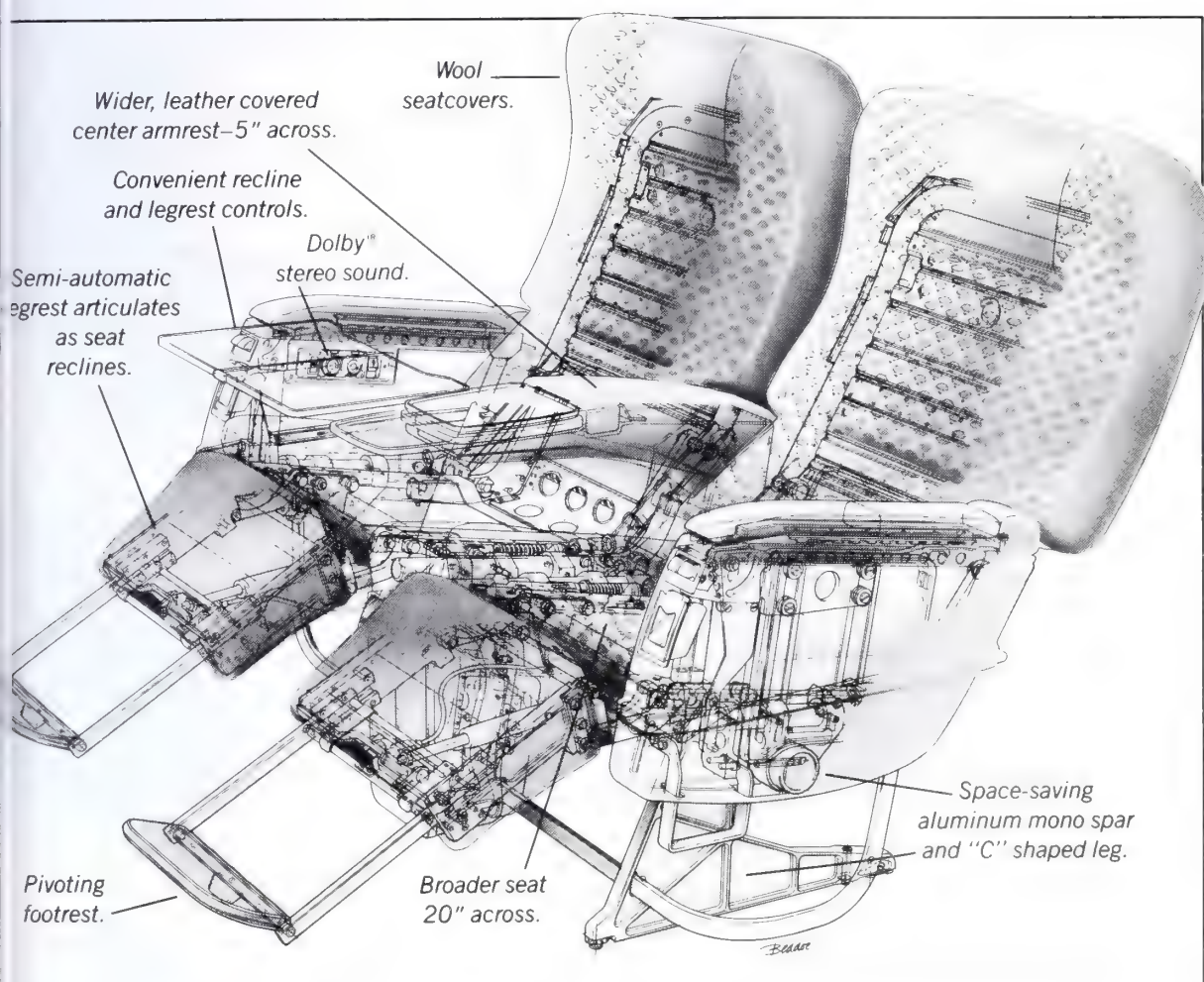
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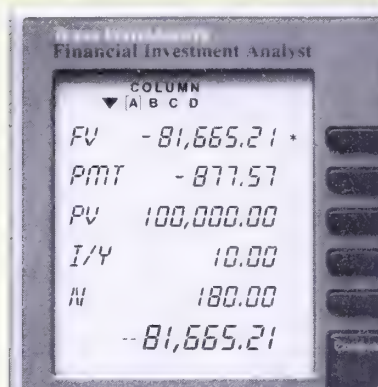
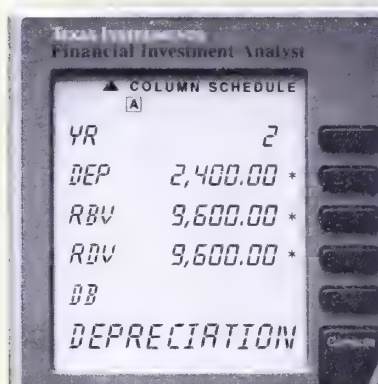
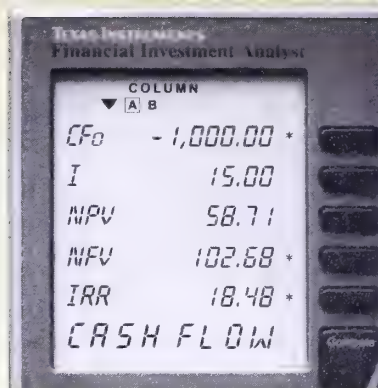
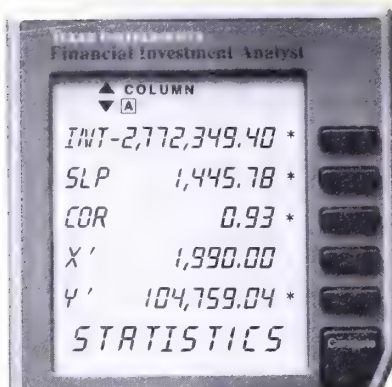
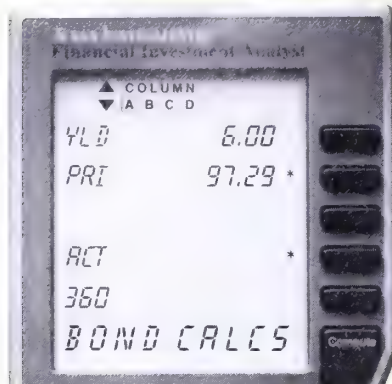
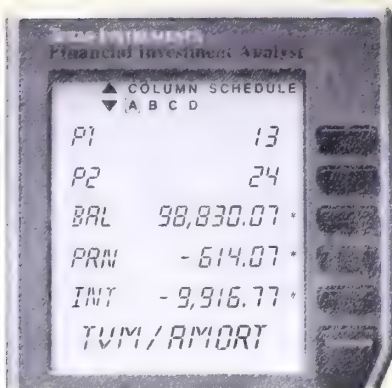
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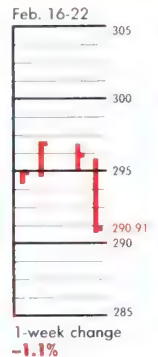
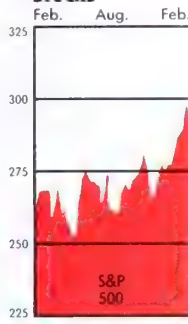


Investment Figures of the Week

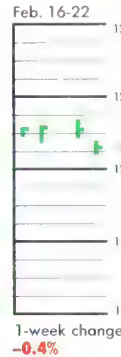
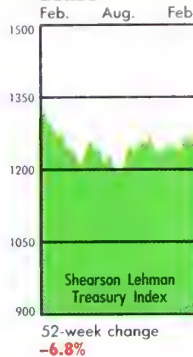
CURRENCY

Inflation is continuing to pressure the financial markets. The dollar slipped, and stocks plummeted, as traders reacted to word of a 1% rise in the January consumer price index. In one sign of easing gloom, the put-call ratio indicator of speculative market sentiment, turned down. However, the market left small companies relatively untouched. Likewise, interest in the dollar did not move much. Gold prices rose, but not much.

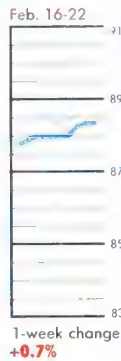
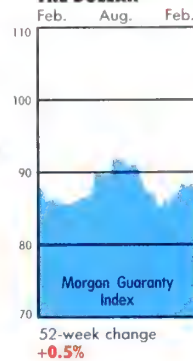
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS

	Latest	% change Week	% change 52-week
DOW JONES INDUSTRIALS	2284.1	-0.9	12.0
DOW JONES COMPANIES (Russell 1000)	154.0	-1.0	10.2
DOW JONES COMPANIES (Russell 2000)	155.4	-0.1	16.5
DOW JONES COMPANIES (Russell 3000)	165.5	-0.9	10.7

IN STOCKS

	Latest	% change (local currency) Week	% change 52-week
DOW JONES INDUSTRIALS (FINANCIAL TIMES 100)	2033.7	-0.7	15.5
DOW JONES INDUSTRIALS (NIKKEI INDEX)	32,311.9	0.5	29.4
DOW JONES INDUSTRIALS (TSE COMPOSITE)	3584.1	-0.7	13.4

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	8.5%	8.5%	5.6%
30-YEAR TREASURY BOND YIELD	9.1%	9.1%	8.4%
S&P 500 DIVIDEND YIELD	3.4%	3.3%	3.2%
S&P 500 PRICE/EARNINGS RATIO	11.8	11.9	15.3

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 26-week moving average	277.4	276.1	Positive
Stocks above 26-week moving average	65.7%	63.5%	Neutral
Speculative sentiment: Put/call ratio	0.24	0.30	Negative
Insider sentiment: Vickers sell/buy ratio	1.03	1.01	Positive

INDUSTRY GROUPS

WEEK LEADERS

	% change 4-week	% change 52-week
ALUMINUM PRODUCTS	19.2	83.9
ALUMINUM	13.7	44.1
REL. MANUFACTURING	9.9	-22.7
ING. MATERIALS	9.5	11.6
RE TIME	8.9	20.1

WEEK LAGGARDS

	% change 4-week	% change 52-week
COMMUNICATIONS EQUIPMENT	-2.3	-11.4
WEIGHT	-1.0	22.7
L. AND GLASS CONTAINERS	-0.7	22.1
NATIONAL OIL	-0.6	6.3
RIC POWER	-0.5	0.7

Strongest stock in group

	% change 4-week	% change 52-week	Price
WEST POINT-PEPPERELL	23.6	88.3	56 1/4
PAN AM	34.8	40.9	3 7/8
VF	13.7	7.1	32 1/4
USG	23.3	1.9	6 5/8
COLEMAN	70.7	100.4	70 5/8

Weakest stock in group

	% change 4-week	% change 52-week	Price
NORTHERN TELECOM	-6.7	-18.3	15 5/8
FEDERAL EXPRESS	-2.1	14.8	51 1/2
CROWN CORK & SEAL	-1.0	52.7	49 1/4
TEXACO	-6.9	17.9	50 1/4
NIAGARA MOHAWK POWER	-10.3	-9.4	12

MUTUAL FUNDS

IS

	%
GLOBAL GROWTH—JAPAN	11.2
A	9.4
TEGIC GOLD/MINERALS	8.9

LAGGARDS

	%
STRATEGIC INVESTMENTS	-5.9
THOMSON MCKINNON PRECIOUS METALS	-5.9
VAN ECK GOLD/RESOURCES	-4.4

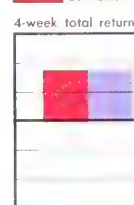
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	%
MANN	68.9
INCE GLOBAL CANADIAN	47.8
MBIA SPECIAL	45.4

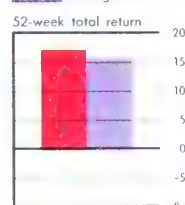
52-week total return

	%
STRATEGIC INVESTMENTS	-35.4
UNITED SERVICES GOLD SHARES	-26.3
STEADMAN OCEANOGRAPHIC TECHNOLOGY	-19.3

S&P 500



Average fund



RELATIVE PORTFOLIOS

Amounts
at the present
of \$10,000
and one year
each portfolio



Foreign stocks

\$13,101

-0.50%



U. S. stocks

\$11,470

+1.18%



Money market fund

\$10,643

+0.16%



Treasury bonds

\$10,286

+0.11%



Gold

\$8,659

-0.16%

In this page are as of market close Wednesday, Feb. 22, 1989, unless otherwise indicated. Groups include S&P 500 companies only; performance and share prices are as of market close.

Feb. 21. Mutual fund returns are as of Feb. 17. Relative portfolios are valued as of Feb. 21. A more detailed explanation of this page is available on request.

NO-FAULT INSURANCE: KEEP IT PURE

The high cost of auto insurance has exploded into controversy, especially in the densely populated states where rates are typically highest of all. Certainly, the regional discrepancies are glaring. A Memphis couple with two teenage sons paid \$2,025 in 1988 for auto insurance for their 1987 Chevrolet Caprice and their kids' 1982 Buick LeSabre. Had the family been living in Los Angeles, the same coverage would have cost \$5,812; in Philadelphia the premium would have reached \$6,992.

In many states, the response to the explosion in auto insurance has been political: demands that state legislatures make affordability a policy goal of the state's insurance regulatory function. Activism reached an extreme in California in November when voters approved Proposition 103, designed to roll back auto rates by 20% and then freeze them for a year. Proponents argued successfully that the automobile is a necessity for most people, and therefore insurance must be affordable. Carried to its logical conclusion, this argument says auto insurance is a de facto utility, and like other utilities it should be guaranteed a fixed return, but no more.

But there is a potentially cheaper, less bureaucratic road toward affordable costs: no-fault auto insurance, under which accident victims are compensated for medical insurance and lost wages by their own insurer, regardless of who was at fault in the accident. In exchange, the insured accepts limits to his right to sue the other party. Although 24 states have adopted some form of no-fault insurance, 10 have no restrictions on victims' rights to bring suits. The essence of a true no-fault system is a meaningful restriction of access to the legal system; many states, such as New Jersey, have learned to their regret that mixing the two systems increases, rather than reduces, claims costs and therefore premiums. The experience of Florida, Michigan, and New York, which all combine no-fault insurance with so-called verbal thresholds that spell out criteria for permitting suits in terms of injuries sustained, is that claims costs and premiums can be lowered. What is needed is some political courage by the lawyer-dominated legislatures to embrace the concept of pure no-fault.

GET READY FOR THE COMPUTER AGE, PART II

It seems almost inconceivable that the computer industry could be maturing. By far the most dynamic American business for much of the postwar era, it has come to represent the triumph of technical innovation, entrepreneurial derring-do, and, in a sense, youth itself. Yet the inevitable is happening: The industry has become so enormous and computers so pervasive that slower growth is all but a certainty (page 68).

The idea of a maturing computer industry, however, not augur trouble for the U.S. economy. Nor will it be the end of technical innovation or set limits to finding ways for businesses and individuals to use computers in the future. On the contrary, technology is reducing computing costs faster all the time, which should make computing accessible than ever. But, paradoxically, it is also a reason behind the decline in overall revenue growth, pushing the industry into a more mature phase.

It's bound to be a painful adjustment, at least in the short term. Analysts predict that slowing revenue growth will provoke a major industry restructuring in the coming decade. That will challenge managers as never before. In the face of riding an enormous wave of demand that has compounded for almost any errors, they'll be forced to plan and execute with a great deal more precision. The price of doing business will become as great as it is in other goods businesses.

Inevitably, however, computer buyers should realize the benefits. The computer makers who prosper will be those that come up with the hardware, software, and services that make computing truly useful. That's when the Information Age will begin for everyone, not just for techies and their corporations.

THE U.S. MUST DEFEND FREE SPEECH—LOUDLY

For Americans accustomed to two centuries of free expression as a constitutional right, the Ayatollah Khomeini has provided a harsh reminder that liberties are always under attack and must constantly be defended. Raged by what he considers to be insults to Islam, Khomeini recently published book, *The Satanic Verses*, Khomeini's effect put out a contract for the murder of author Salman Rushdie, an Indian-born British citizen, and its publication including Americans. Khomeini's public incitement to violence by religious fanatics could put thousands of book publishers' and publishers' employees in jeopardy all over the world.

What Khomeini offers is a glimpse of anarchy. To forestall this threat, and to forestall others that will follow if Khomeini's is not squelched, governments and private citizens must mobilize political and economic counterpressure as well as moral protests. European Community member states the way with an unprecedented agreement on Feb. 12 to recall all 12 of their envoys from Tehran. That action by the EC warned Iran that its ties with Western Europe, badly needed to rebuild its war-shattered economy, will be jeopardized if Khomeini does not desist. By contrast, the new Administration of President Bush was remarkably slow to react, and its eventual comments were tepid generalities rather than a ringing defense of freedom of expression. Although the U.S. has little direct leverage over Iran, Washington must make clear that its full resources will be committed to protecting Americans against Khomeini's threat. With that assurance, Americans should not hesitate to exercise their right to publish, sell, buy, read, and discuss the book.

ALS IN
COMMUNICAL
PAGE 138

BusinessWeek

MARCH 13, 1989

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THE TRILLION DOLLAR MAN

Budget Director
Dick Darman
wants to do
more than cut
the deficit. He
wants to reshape
America. And
he's not kidding.

PAGE 100



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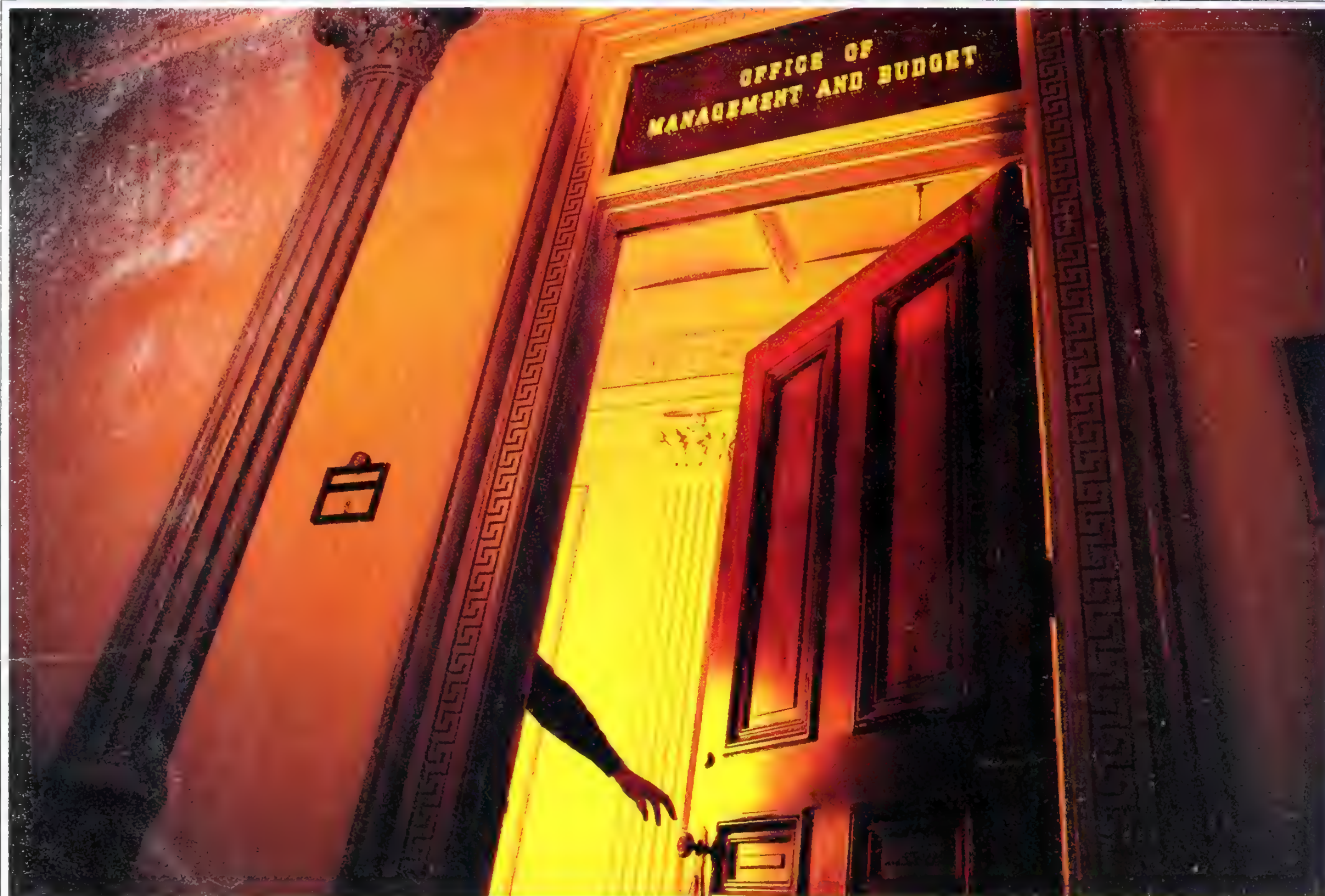
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DOOR OF OPPORTUNITY: VIRTUALLY EVERY DOMESTIC INITIATIVE PASSES THROUGH THE OMB—GIVING DARMAN HUGE PUBLIC POLICY CLOUT

Cover Story

100 THE TRILLION-DOLLAR MAN

Tame the deficit? No problem. Budget chief Richard Darman is confident on that point—and most others. His dream: To cure the 'corpocracy' of shortsightedness. Darman brings a brilliant mind and solid credentials to a tough job. But with Democrats sniping and possible conflicts with such Bushmen as Brady and Sununu, he may need a talent for bridge-building most of all

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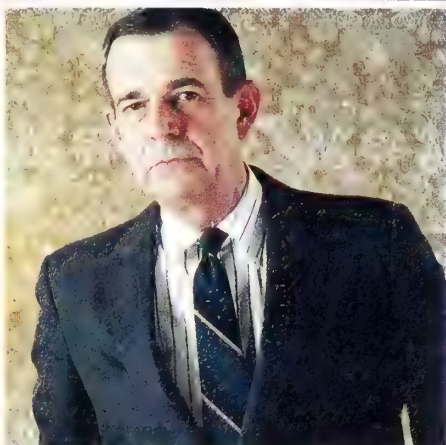
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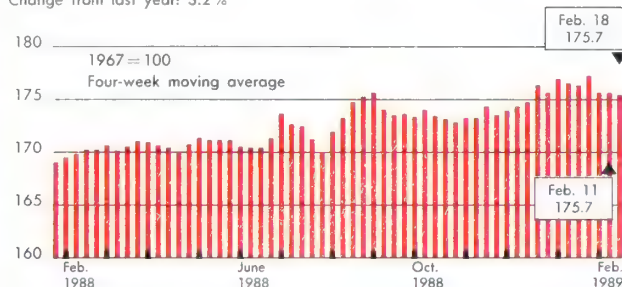
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Speed up Latin debt write-offs
There's no 'right' to bear Uzis

BusinessWeek Index

PRODUCTION

Change from last week: 0.0%
Change from last year: 3.2%

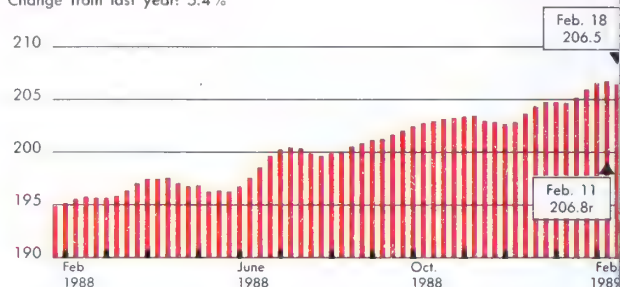


The production index was unchanged for the week ended Feb. 18. The index has been flat so far in February. On a seasonally adjusted basis, production of lumber, coal, autos, rail-freight traffic, and paper posted increases. This was offset by declines in electric power, crude-oil refining, steel, trucks, and paperboard output. Prior to calculation of the four-week moving index, the index declined to 176.9 from 177.4 in the previous week.

BW production index copyright 1989 by McGraw Hill Inc.

LEADING

Change from last week: -0.1%
Change from last year: 5.4%



The leading index dropped slightly for the week ended Feb. 18. On the negative side, stock prices were lower and bond yields were higher. Faster growth in materials prices and real estate loans provided the positive signals. The M2 growth rate was unchanged, and data on business failures were unavailable for the week. Before calculation of the four-week moving average, the index increased to 206.1 from 205.6 for the week before.

Leading index copyright 1989 by Center for International Business Cycle Research

PRODUCTION INDICATORS

	Latest week	Week ago	% Change year ago
STEEL (2/25) thous. of net tons	1,972	2,008 #	-0.7
AUTOS (2/25) units	148,464	157,768r #	13.6
TRUCKS (2/25) units	89,867	95,205r #	5.9
ELECTRIC POWER (2/25) millions of kilowatt-hours	55,761	55,247 #	6.9
CRUDE-OIL REFINING (2/25) thous. of bbl./day	12,699	12,933 #	0.2
COAL (2/18) thous. of net tons	19,351 #	17,951	3.6
PAPERBOARD (2/18) thous. of tons	738.5 #	738.9r	-2.6
PAPER (2/18) thous. of tons	741.0 #	722.0r	-1.5
LUMBER (2/18) millions of ft.	454.9 #	364.2	-14.2
RAIL FREIGHT (2/18) billions of ton-miles	19.6 #	19.1	6.5

Sources: American Iron & Steel Inst., Ward's Automotive Reports, Edison Electric Inst., American Petroleum Inst., Energy Dept., American Paper Inst., WWPA¹, SFPA², Association of American Railroads.

FOREIGN EXCHANGE

	Latest week	Week ago	Year ago
JAPANESE YEN (3/1)	128	127	129
GERMAN MARK (3/1)	1.84	1.84	1.69
BRITISH POUND (3/1)	1.72	1.75	1.77
FRENCH FRANC (3/1)	6.25	6.26	5.71
CANADIAN DOLLAR (3/1)	1.20	1.20	1.26
SWISS FRANC (3/1)	1.57	1.57	1.40
MEXICAN PESO (3/1) ³	2,353	2,341	2,300

Sources: Major New York banks. Currencies expressed in units per U. S. dollar, except for British pound expressed in dollars.

PRICES

	Latest week	Week ago	% Change year ago
GOLD (3/1) \$/troy oz.	384.050	386.750	-10.5
STEEL SCRAP (2/28) # 1 heavy, \$/ton	123.00	123.00	3.4
FOODSTUFFS (2/27) index, 1967=100	232.4	232.2	6.4
COPPER (2/25) ¢/lb.	144.8	134.3	41.7
ALUMINUM (2/25) ¢/lb.	102.0	98.5	-1.0
WHEAT (2/25) # 2 hard, \$/bu.	4.40	4.35	36.2
COTTON (2/25) strict low middling 1-1/16 in., ¢/lb.	55.35	54.79	-2.9

Sources: London Wed. final setting, Chicago mkt., Commodity Research Bureau, Metals Week, Kansas City mkt., Memphis mkt.

Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment.
1 = Western Wood Products Assn. 2 = Southern Forest Products Assn. 3 = Free market value NA = Not available r = revised NM = Not meaningful

LEADING INDICATORS

	Latest week	Week ago	% Change year ago
STOCK PRICES (2/24) S&P 500	291.52	294.03	10
CORPORATE BOND YIELD, Aaa (2/24)	9.70%	9.65%	4
INDUSTRIAL MATERIALS PRICES (2/24)	102.6	102.5	5
BUSINESS FAILURES (2/17)	NA	NA	NM
REAL ESTATE LOANS (2/15) billions	\$312.7	\$311.5	13
MONEY SUPPLY, M2 (2/13) billions	\$3,081.2	\$3,078.6r	7
INITIAL CLAIMS, UNEMPLOYMENT (2/11) thous.	326	281	0

Sources: Standard & Poor's, Moody's, Journal of Commerce (index: 1980=100), Dun & Bradstreet (failures of large companies), Federal Reserve Board, Labor Dept. CIBCR seasonally adjusts data on business failures and real estate loans.

MONTHLY ECONOMIC INDICATORS

	Latest month	Month ago	% Change year ago
CONSTR. SPENDING (Jan.) annual rate, billions	\$424.0	\$422.3r	7
PERSONAL INCOME (Jan.) annual rate, billions	\$4,282.0	\$4,208.0r	9
ORDERS FOR DURABLE GOODS: MFG. (Jan.) billions	\$128.1	\$132.1r	13
AGRICULTURAL PRICES (Feb.) index, 1977=100	148	149	13

Sources: Census Bureau, Commerce Dept., Dept. of Agriculture

MONETARY INDICATORS

	Latest week	Week ago	% Change year ago
MONEY SUPPLY, M1 (2/13)	\$784.0	\$787.2r	4
BANKS' BUSINESS LOANS (2/15)	311.0	310.0r	9
FREE RESERVES (2/22)	670	1,082r	-2
NONFINANCIAL COMMERCIAL PAPER (2/15)	108.2	107.9	30

Sources: Federal Reserve Board (in billions, except for free reserves, which are expressed in a two-week period in millions).

MONEY MARKET RATES

	Latest week	Week ago	Year ago
FEDERAL FUNDS (2/28)	9.87%	9.33%	6.60
PRIME (3/1)	11.50	11.00	8.50
COMMERCIAL PAPER 3-MONTH (3/1)	9.86	9.44	6.51
CERTIFICATES OF DEPOSIT 3-MONTH (3/1)	10.00	9.60	6.58
EURODOLLAR 3-MONTH (2/22)	9.68	9.58	6.75

Sources: Federal Reserve Board, First Boston



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looks at it, he smiles. Very popular
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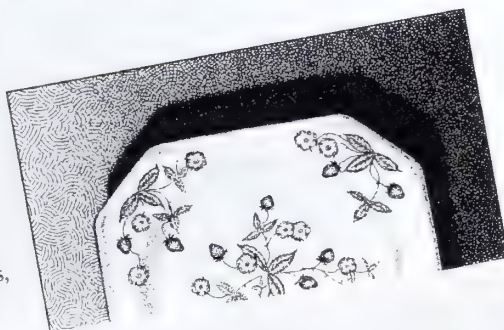
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BFGoodrich
Chemicals and Aerospace

Readers Report

economic and tax matters to judge if a lower capital-tax rate would produce jobs and other advantages—experts are of different minds about it—but I know that a capital-gains tax that is not indexed for inflation is a fraud. This is particularly applicable to older citizens, who live mostly on fixed incomes in an era of continuous inflation and at times find it necessary to dip into their life savings. They frequently find that when assets held for a long time are sold, there is a loss instead of a gain in real, inflation-adjusted dollars.

At present there is some talk about applying the capital-gains tax to inheritances. Many inherited assets are held for long periods and have appreciated in inflated dollars. Here, too, a capital-gains tax without indexation for inflation is a government fraud.

Victor Alin
Wayne, Pa.

In your editorial you state: "The present system grossly overtaxes long-range investment." It certainly does for those of us who are retired and try to protect the safety of principal by changing investments.

The "gain" may move us into a bracket

where some of our Social Security benefits become taxable or the tax is increased for those already having their benefits chipped away. Further, starting in 1989 the tax on the gain and on the Social Security benefit will be included in determining our medicare supplemental premium. And in my state there is a push on to double the capital-gains tax.

Who's kidding whom?

John F. Elsbree
Brighton, Mass.

THE S&L CURE MAY BE WORSE THAN THE DISEASE

Regarding "Bush's S&L plan: Full of good intentions—and holes" (Top of the News, Feb. 20): BUSINESS WEEK truly treats President Bush in a gentler and kinder way in discussing his plan to bail out ailing thrifts. To issue \$50 billion in 30-year bonds is simply to increase the national debt, a commitment to pay for an immediate problem over the next 30 years. It is absurd to take 30 years to pay for the problems that developed in less than a decade. Most of the S&Ls may not survive long enough to participate in paying off this enormous debt.

Although criminal activity and sheer

incompetence appear to have been important factors in this debacle (and those guilty of criminal wrongdoing should be punished to the full extent of the law, and their injury to the taxpayer was enormous), the main blame must be laid at the doors of Congress and the Administration. It is therefore mainly the taxpayers who should assume the burden of paying the costs of cleaning up this problem. Loading too much of the burden on the surviving S&Ls will hasten their demise. The banks may be in a better position to help, but it is grossly unfair and discriminatory to impose much of the burden on them.

Even the figures quoted in BW—\$36 billion in interest over the first 10 years on a \$50 billion issue—are incredibly optimistic. Who will buy 30-year bonds yielding about 7%?

Frank Johnson
Dallas

I have been watching the media for a clear-cut explanation as to why many S&Ls are insolvent. At first I explained this away as a symptom of "oil-patch sickness," but as it spread in otherwise economically healthy territories, additional explanation is required. Ho-

NORTHWEST

STANDARD OFFICE SUPPLIES IN HONG KONG. A DESK, A CHAIR, A PHONE AND A FISH.

It all seems a little strange when you first start doing business in Hong Kong. Customs are different and the right fish in the right place is as important as the right memo at the right time.

FUNG SHUI MAN It's pronounced "fung soy" and he's a religious man who tells you when is the best time to move into a new office, where to have your desk and whether or not you need a goldfish for the atmosphere it will provide. If you open a new office in Hong Kong, ask your business contacts to recommend their "man." Hire the most

expensive one you can find. Skimping on the spirits will only give you a bad business reputation.

GRILLED AT THE GRILL The famous Mandarin Grill at the Mandarin Hotel is "the" place for the important meetings in Hong Kong. The view is quite spectacular and the wine list is impressive. The service is exquisite and the food can only be described as sublime. Tel. 5-220111.

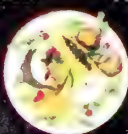
HOW TO KILL YOUR FIRST BIG MEETING

Even during the summer months, business dress should always

be proper—suits and ties. Informal attire is not appreciated. Also, in Hong Kong, the color red is a symbol of happiness.



NORTHWEST NOTES In addition to convenient service to Hong Kong from over 200 U.S. cities and, starting in June, nonstop service from Seattle on our new Boeing 747-400 widebodies—we give you something no other U.S. airline can offer—the knowledge, information and insight that comes after 40 years of helping people do business in Asia.



LOOK TO US NORTHWEST AIRLINES

out this from a layman's viewpoint: First, tax laws are modified to include benefits for owning S&Ls. Result: We begin to get S&Ls on every street corner. Second, we deregulate S&Ls. Result: They begin to make loans in areas in which they have little experience.

Third, in an effort to rob Peter to pay Paul, we pass the tax law of 1986, which moves all tax loophole incentives for financing commercial property. The result has been a 20% to 30% devaluation in the prices of some real estate. Those S&Ls that had lent at the pre-tax-law appraisals now face owners who no longer want their properties. Result: S&Ls are getting huge inventories of properties whose mortgages exceed their value.

In conclusion, we are getting more tax dollars from the real estate industry now than before 1986, but those dollars are going to have to be used to bail out S&Ls. Surely some econometric model could have anticipated this.

Robert H. Ingalls
Albuquerque

Danny Wall's pallid apologia, "Selling sick thrifts is the lesser of two evils" (Readers Report, Feb. 6), for his perilous decision to sell off 34 insolvent thrifts at fire-sale prices to some future capitalists uses an entirely eco-

nomie rationale. Like so many in the Reagan Administration, he places no weight on fairness, justice, or ethics. His actions will enrich well-heeled companies and individuals through the provision of enormous tax write-offs, and will prop up marginal operations in an already oversaturated market.

Ordinary taxpayers and small depositors, on the other hand, are likely to end up poorer by being forced to pay, one way or another, to restore the savings industry to health—yet another instance of government punishing the innocent and rewarding the guilty.

Before that happens, I would like to see some action taken to correct the excesses that led to this debacle and some appropriate action taken against those responsible. The list is long and includes somnambulant regulators, avaricious depositors, indifferent members of Congress, imprudent thrift management, and self-serving accountants.

Robert B. Morgan
Fairfield, Conn.

A GUILTY CORPORATION SHOULD HAVE TO PAY THE PIPER

You printed a letter from an Allan D. Graves that requires a rebuttal ("Punish the arms swindlers, not stock-

holders," Readers Report, Feb. 13).

His premise is that shareholders are not responsible for acts of overbilling by corporations, committed no crimes, and thus should not be "punished by having a fine levied against a corporation whose stock they own.

Graves concludes that CEOs and directors should be fined instead. However, he ignores the fact that they too may be as innocent as shareholders.

I am a director of a number of public companies and I can assure your readers that directors do not personally approve every bill rendered.

In overbilling situations, those found guilty of a crime should be dealt with under the law, those found innocent should be left alone. The premise of finding the "corporation" is that it benefited from the prior overbilling, and this makes sense.

If shareholders are unhappy, they hold the "ultimate weapon," the ability to fire the board of directors.

Alan H. Weingarten
Ramsey, N. J.

Letters to the Editor should be sent to Readers Report, Business Week, 1221 Avenue of the Americas, New York, N. Y. 10020. Fax: (212) 512-6875, Telex: 12-7960, Intl. 4998204. All letters must include an address and daytime and evening telephone numbers. We reserve the right to edit letters for clarity and space.



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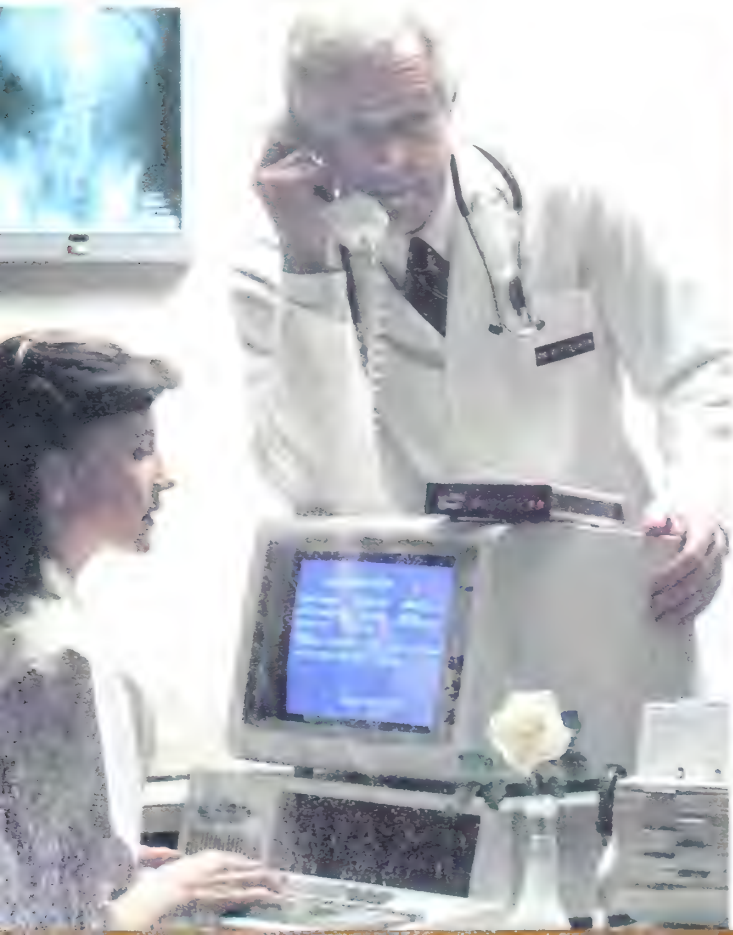
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WEST OF EDEN: THE END OF INNOCENCE AT APPLE COMPUTER

By Frank Rose

Viking • 356pp • \$19.95

APPLE'S PAINFUL PASSAGE TO ADULTHOOD

In 1983 no company better exemplified capitalism with a mission than Apple Computer, Silicon Valley's most precocious child. Steve Jobs, Apple's chairman and co-founder, lured John Sculley, the president of Pepsi-Cola, to Apple by mixing an insult with a tantalizing promise: If Sculley would stop selling sugar water, he could help change the world by putting that great democratizing instrument, a personal computer, in every home. Though heir-apparent to Pepsi's chairmanship, Sculley took the bait, traded his pinstripes for khakis, and headed for the Coast.

Thus began one of Corporate America's most bizarre and tempestuous relationships. Sculley was hired as Apple's president to balance Jobs's messianic vision with pragmatism and consumer marketing expertise. At first the two

were nearly inseparable, and Sculley often deferred to Jobs's thinking. In fact, at his first anniversary dinner, he announced: "As far as I'm concerned, Apple has only one leader: Steve and me." Nonetheless, by September, 1985, after an ugly power struggle, Sculley, with the board's support, had forced Jobs out.

West of Eden: The End of Innocence at Apple Computer by New York journalist Frank Rose, opens with Sculley's arrival. Rose does flash back to recount Apple's 1976 birth in a garage. But most of the book chronicles the wrenching changes at Apple, by then a \$1 billion corporation, that led to Jobs's departure.

Rose took a risk by investing three years in a subject already heavily reported. In addition to hundreds of newspaper and magazine accounts, four other Apple books have been published, including

Sculley's less-than-objective 1987 memoir. Of them all, *West of Eden* seems most likely to endure as the definitive account of the convulsive period that saw Apple grow up. (I should say here that I also have written extensively about Apple, and that Rose, a professional acquaintance, names me in his lengthy acknowledgments, apparently because I discussed the company on one occasion.)

To present the ultimate insider's perspective, Rose climbs in and out of the heads of various characters. For the most part, the device works. His smooth and lively story captures better than any previous attempt the spirit of Apple under Jobs. But the book's most notable weakness is Rose's lack of access to Jobs, who spent only an hour with Rose before declining further interviews. Undaunted, Rose relied on several of Jobs's closest friends and colleagues.

Rose seems to have had only a little more luck getting to Sculley, so that the book's perspective is at times too easily framed by the people to whom Rose has greatest access. Those who, in Rose's view, played a large role in some crucial operating decisions were Mike Murray, the Macintosh marketing manager; Ed Belleville, the Macintosh engineering

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tor; and Jay Elliot, Apple's person-
director. At one critical juncture,
en Apple was in disarray, Rose
ites, Elliot was in effect running
company. That's unlikely to have
en true, except perhaps in Elliot's
agination. Eventually all three men
re forced out.

Rose's tone is authoritative and
y. He's not afraid to poke a little
at people who are a bit too seri-
s about such goals as "facilitating
sonal growth" and "shifting para-
ms"—classic Applespeak for reor-
ing the way one looks at the
rld. After all, Jobs & Co. owe their
tastic early success to the mun-
e business of manufacturing a
puter people wanted, getting it
o stores, and maintaining extraor-
ary profit margins.

Jobs, in particular, is often exposed
the sharp edge of Rose's wit. After
ving Apple, Jobs briefly considered
eking office, Rose writes. "Steve
d long fantasized about entering
itics on the John Kennedy model, tak-
over the government, straightening
the bureaucracy.... It was too bad
d never registered to vote. But Steve
s able to look beyond that as a prob-
l.... A bigger difficulty was that he
n't know which party to run under.



SHARED DELUSIONS: JOBS AND SCULLEY IN 1984

Maybe he could offer himself to both."

Rose not only manages to weave these
events into a seamless tale but also pre-
sents some fresh news. He offers new
details about Jobs's overtures to Don
Estridge, then head of IBM's Entry Sys-
tems Div., before he turned to Sculley.

He tells of venture capitalist Ben Ro-
sen's attempt to sell Compaq Comput-
er to Apple in 1985. Then there were
the curious plans, hatched by Jobs
and Sculley, to sell part of Apple to
General Motors, General Electric, or
AT&T and then finance the purchase
of a company far larger than Apple,
such as Xerox.

In outlining these schemes, which
went as far as meetings with the pro-
jected partners, Rose argues that
shared delusions kept Sculley and
Jobs in each other's thrall until it was
nearly too late. The Macintosh, born
in 1984, manifested Jobs's vision of
"One person, one computer." But ear-
ly versions were underpowered and
had limited software, and by early
1985, Apple was choking on inven-
tory. Jobs grew wary of Sculley, who
was, after all, just a marketing guy.
And Sculley, deciding that he had lis-
tened too long to Jobs, stripped him
of all operating responsibilities.

More than the blossoming and
souring of this friendship, *West of Eden*
tells of a group of quixotic Californians
whose dream collided with business real-
ity. But Apple was never as innocent as
the subtitle suggests. Jobs is an impas-
sioned idealist with an uncanny ability to
adapt technology for popular use. But it

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Books

was publicist Regis McKenna who saw Jobs's charismatic side and made it larger than life. It was McKenna who exploited the image of inspired, jeans-clad kids having fun and building, in Jobs's phrase, "insanely great" computers. The truth, almost from the start Apple's financial strings have been pulled by conservative venture capitalists and even more conservative board members. They insisted that someone like Sculley be hired in the first place. And, in the end, they turned their backs on Jobs.

BY KATHARINE M. HAFNER

Hafner, a former BUSINESS WEEK staff writer, is writing a book on computer hackers.

BOOK BRIEFS

MACY'S FOR SALE: THE LEVERAGED BUYOUT OF THE WORLD'S LARGEST STORE

By Isadore Barmash

Weidenfeld & Nicolson • 172pp • \$19.95

As the largest leveraged buyout in the retailing industry, the \$1.5 billion management acquisition of R. H. Macy & Co. was watched with great interest by retailers, corporate chieftains, and investment experts alike. But Isadore Barmash, longtime retail reporter for *The New York Times*, has failed to turn the 1986 deal for the venerable chain into a compelling book.

Macy's For Sale is devoid of wit, personality, or juicy detail. Barmash has made up for the lack of cooperation of Macy's top executives, in particular the central character, Chairman Edward S. Finkelstein.

Barmash credits Finkelstein, a career Macy's man, with turning the dowdy chain into a hip, theatrical business aimed at more affluent shoppers. He also paints Finkelstein as arrogant, impatient, and egotistical, a man whose main motive for going private was to enrich himself and his cronies.

While Finkelstein has insisted that the LBO energized Macy's by giving 350 employees a greater personal and financial stake, Barmash suggests that the company was not helped. He quotes former Vice-Chairman David L. Yunis: "Macy's... has cut a lot of people. It milked the assets of the company to load itself up with debt. Who's benefited from the deal? The answer is obvious."

With such Macy's rivals as Federal Department Stores succumbing to unwanted takeovers, going private may have been the right choice. But lately Macy's has been awash in red ink. Ironically, *Macy's For Sale* leaves readers hanging. Though Barmash has put the story between hard covers, the final chapter has yet to be written.

BY AMY DUNN

BusinessWeek Travel Facts

DID YOU KNOW? In 1989, BUSINESS WEEK will publish two Business Travel Sections authored by Steve Birnbaum. Issue dates: April 24 and October 30. For more information call your BUSINESS WEEK Representative or John Holden at 212/512-6394.



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Despite the growth of two-income families in America, a median-priced home today will absorb nearly 50% more family income than it did in 1968.

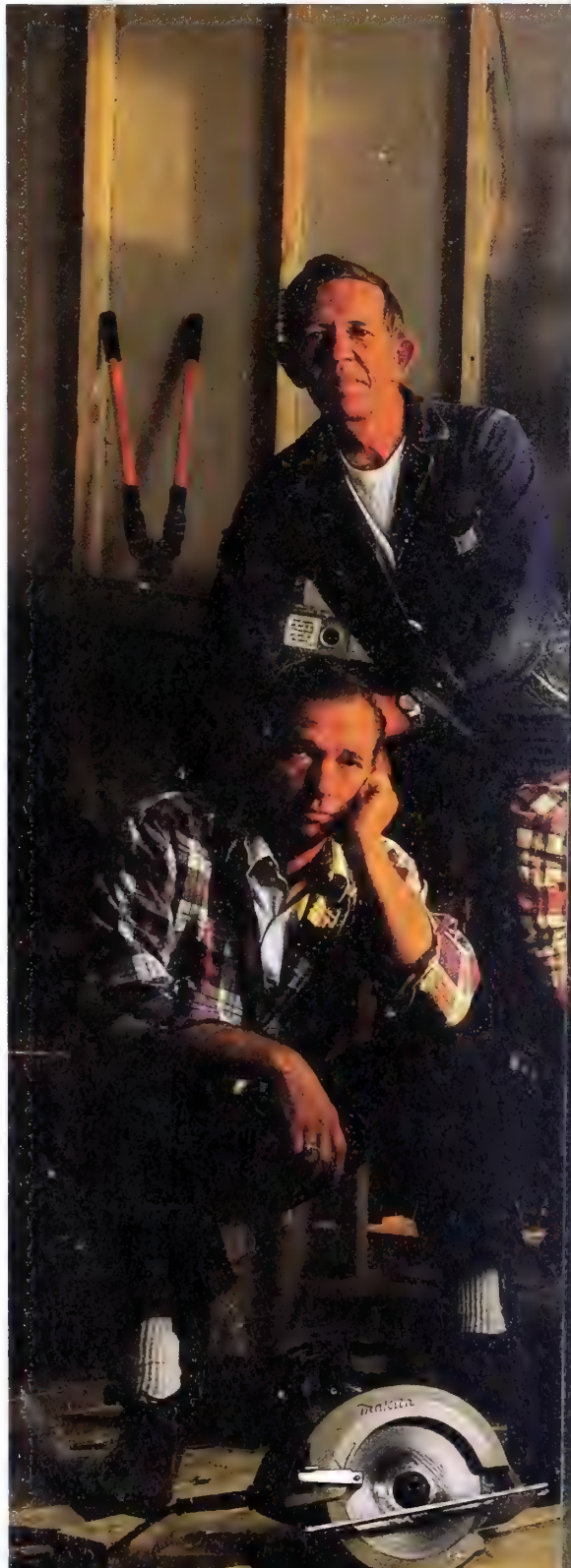
So, is the American Dream becoming a thing of the past for the average American?

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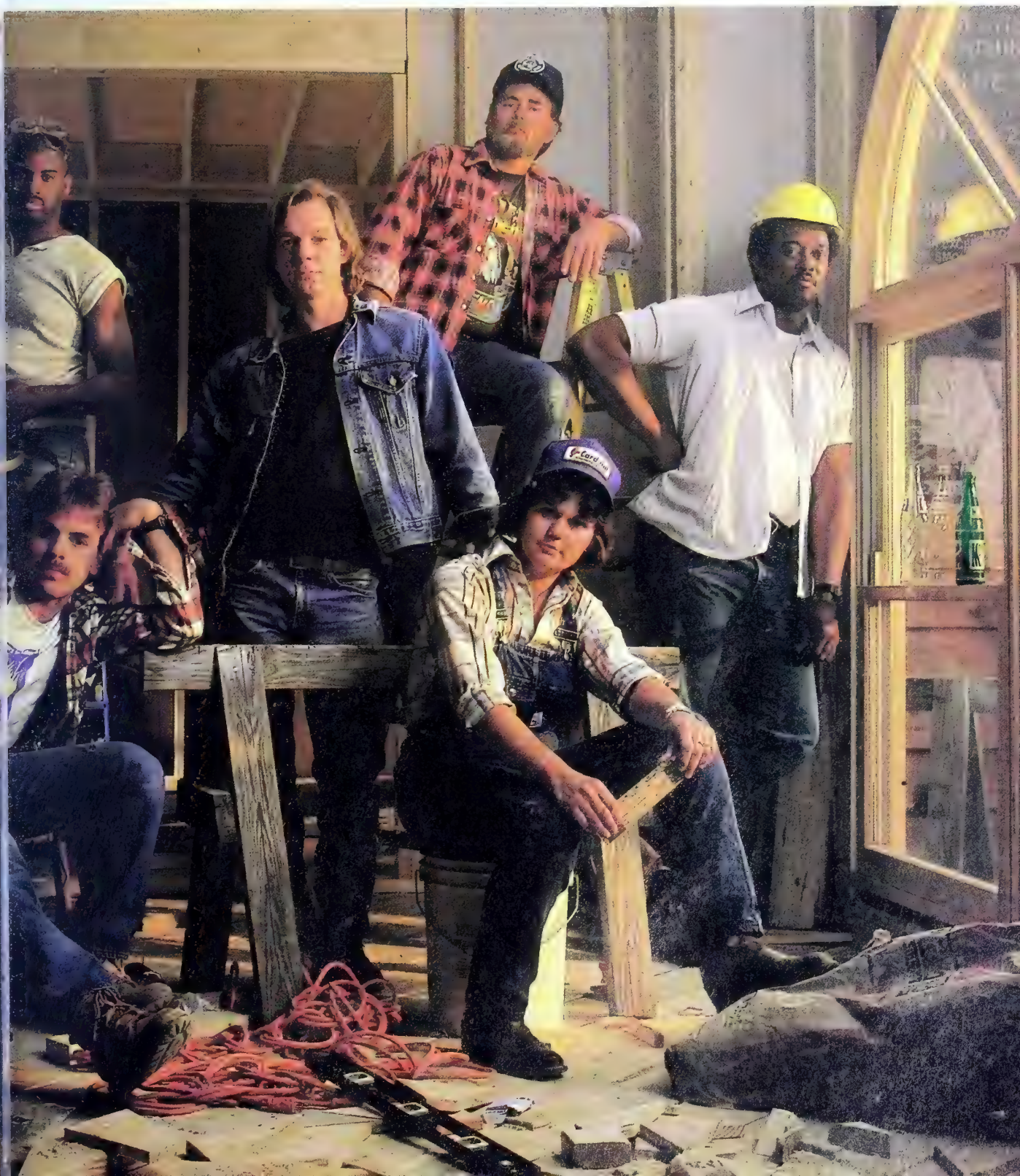
Last year, the average mortgage we financed was \$76,000. But nearly a quarter were for \$40,000 or less, about what it takes for a household with an income of \$19,000 to buy a home.

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Build America's Homes. Can You Afford One?



MAKE THE PUNISHMENT FIT THE CORPORATE CRIME

BY GARY S. BECKER



Fines should be based on the harm done to individuals, other organizations, and society at large. To compensate for those companies that get away with crimes, the penalty should be a multiple of the damage done

What is the rational way of setting proper punishments for business crimes? The Drexel Burnham Lambert Inc. plea-bargaining agreement that is said to impose a fine of more than \$600 million for alleged mail and security fraud is the most current dramatic example of the policy dilemma confronting those who determine punishments, particularly fines. Fines are attractive in these cases because they compensate for damage and punish perpetrators at the same time.

Punishments for corporate crimes—indeed for all crimes—should include fines determined by the harm done to individuals, other organizations, and society at large. The penalty should be a multiple of, rather than simply equal to, the harm caused. That is because many violators of the law go unpunished. If companies that are convicted pay only for the damages they cause, the deterrent effect of fines would be too weak, because companies that are not caught pay nothing.

CAUGHT IN THE ACT. The deterrent effect strikes the right balance only if convicted corporations also pay for companies that are not caught. For example, if it is known that only a third of a particular kind of security fraud is punished, those companies convicted of this kind of fraud should pay three times the damage they cause.

It might seem unfair to make convicted companies pay for the crimes of others. But companies that are committing crimes clearly assume that the odds are they won't be caught. Therefore, companies fined according to this formula do not overpay: In the security fraud example, guilty companies have a one-third chance of being caught and paying three times the damage they cause, and a two-thirds chance of escaping punishment and paying nothing.

Obviously, it is hard to estimate damages for many company crimes and even harder to determine the probability of conviction. However, these difficulties are shared by any system that tries to make the punishment fit the crime. Over time, estimates of damages and the likelihood of conviction will improve as the courts and others gain experience in this approach.

It may seem strange that the recommended fines do not depend on the gain from crimes. This is no oversight. The goal is proper deterrence, not vengeance. The object is to eliminate crimes that impose bigger costs on everyone else than the gains to perpetrators. This aim is accomplished with fines that are based only on the harm caused others.

Consider a steel plant that pollutes the water and general environment in the surrounding neighborhood. If each ton

of steel produced causes an illegal environmental damage worth \$100 to the neighbors, and if the probability of conviction for this pollution is one out of four, the appropriate fine should be \$400 per ton produced.

Anytime there is a fine, there is always a chance the profit may exceed the fine. But this is not necessarily bad. In this example, the plant would still make \$100 per ton after paying the fine if it profited by \$500 per ton from the steel production. However, this net profit comes from the steel that people want, not from the damage that has been made to the environment.

I proposed this approach in an article published more than 20 years ago. It was endorsed in a discussion draft of a business crime prepared last July by some members of the U.S. Sentencing Commission. The U.S. Supreme Court recently upheld the legality of this commission, which was created in 1984 by Congress to promulgate sentencing guidelines for federal crimes.

The commission's discussion materials include preliminary estimates of the social harm of and appropriate fines for various crimes. Although these fines are many times those currently imposed by federal courts, the commission tries to avoid excessive punishment by suggesting an allowance for any fines paid in civil suits brought by victims. Even so, the commission may have overstated the harm caused by some perpetrators of business crimes, as a few critics have claimed.

NO JAIL TIME. If there are appropriate fines, there is no reason to jail officials of corporations that commit security fraud, antitrust violations, tax evasion, and similar crimes. Directors of companies that pay large fines for crimes committed by their officials have an incentive to fire them or force them to clean up their act. Imprisonment is inferior to fines because prisons are costly to maintain. In effect, imprisonment punishes taxpayers as well as criminals. Of course, officials should be jailed when their companies engage in murder and other heinous crimes that cannot be compensated for with fines.

Many companies oppose a rational approach to the punishment for business crime out of fear that it will lead to severe penalties. Proper fines are hard for business crimes that cause major harm, but they are mild for the many crimes that have small harmful effects on others. Executives—as well as the public—who take the long view should support the members of the Sentencing Commission who are trying to put punishment of company crimes on a sound footing.

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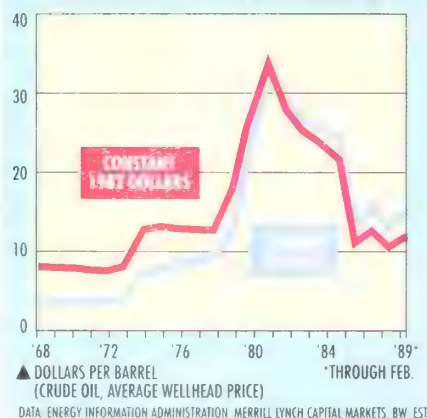
The right choice.

BY GENE KORETZ

OIL IMPORTS ARE SETTING AN AMBUSH FOR THE ECONOMY

The chances are growing that a rising oil import bill will seriously retard improvement in the trade balance in 1989 and beyond. Consider the following: Net U.S. oil imports last year came to almost \$39 billion, roughly a third of the trade deficit. So far this year oil prices have been running about 10% above year-earlier levels. At the same time, import volume in January was up 16%, as consumption rose 2% and U.S. domestic oil output fell 4% from January, 1988,

REAL OIL PRICES ARE NEAR A 15-YEAR LOW



according to government statistics.

Even if they moderate, such trends spell a rising oil-trade deficit. Indeed, the continuing strength of oil prices (thanks in part to OPEC's unexpected discipline), plus the likelihood that a cyclical slowdown in domestic demand won't really hit until next year, have induced economists at Data Resources Inc. to predict that the oil import bill will jump by \$6.2 billion, or 16%, this year. As a result, they say, the overall trade deficit will show little, if any, improvement.

The real oil problem, however, is likely to surface in the years ahead. Despite the hefty 30% increase in oil prices since October, such prices on a real inflation-adjusted basis are not only dramatically below their 1981 peak but also are still beneath their 1974-78 average (chart). And the impact of the sharp decline in real oil prices since 1981 on U.S. production, consumption, and imports is only beginning to make itself felt.

One omen is an oil industry estimate that U.S. imports of oil and petroleum products in January exceeded domestic

oil output for the first time in a decade. Another is statistics indicating that U.S. energy efficiency, defined as the ratio of energy use to national output, probably declined last year after improving by 24% since 1976. In short, weak oil prices have apparently begun to stimulate demand and undo some of the conservation efforts of earlier years while reinforcing the slump in domestic output.

That is precisely the prediction of an econometric study by Federal Reserve Bank of Dallas economists Stephen P. A. Brown and Keith R. Phillips in the latest issue of the bank's *Economic Review*. Their model indicates that it takes U.S. and world consumers nearly a decade to adjust demand to changes in oil prices. Thus they note that the sharp 1979-81 runup in prices caused oil demand to decline during much of the 1980s even though prices were tumbling. In the first quarter of 1988, for example, world oil consumption was about 56 million barrels per day—almost exactly its level eight years earlier. Yet prices had fallen from \$48.64 per barrel (in 1988 dollars) to \$15.47 in the same period, and the world economy had grown substantially.

Now, however, Brown and Phillips' model indicates that demand should start to move higher in response to the more recent decline in real prices and should accelerate sharply within the next two or three years. They find no evidence that the price elasticity of demand is asymmetrical—that is, that oil usage declines in response to higher prices but is relatively unresponsive to lower prices. "The adjustment process is slow," says Brown, "but the recent trend toward larger, less fuel-efficient cars is a sign that it does take place."

Barring a recession, the two economists think world oil consumption will be pressing on capacity by 1993. And they expect oil prices to move sharply higher, reaching \$30 to \$40 a barrel (in 1988 dollars) by the year 2000.

TWO FOREIGN REAL ESTATE BOOMS THAT ARE COOLING DOWN FAST

Two of the most buoyant real estate markets overseas have started to crack. Economist Deborah Allen of the Claremont Economics Institute reports that Tokyo land prices, which doubled between 1985 and 1987, are down 20% to 30% from their peak. A capital-gains tax on short-term transactions and new limits on bank lending for land purchases have helped to burst what had clearly become a speculative bubble, she says.

Meanwhile, high interest rates have

cut home sales in Britain, causing price to level off and even decline in some areas. After booming in 1987 and 1988, home prices could fall sharply this year, says Morgan Grenfell & Co. The British investment firm sees a 20% gap between prices and personal income trends.

INSIDERS ARE STILL BUYING STOCKS AS FAST AS THEY SELL THEM

In the wake of the 1987 stock market crash, corporate insiders went on an unprecedented buying spree, buying about three times as many stocks as they sold. But though insider buying has since simmered down, it is still stronger than the "normal" situation in which sales outnumber purchases. In January reports Brick Securities, about an equal number of issues were bought and sold by insiders, suggesting "little concern about the market outlook."

IS A DOLLAR CRISIS ON THE WAY? THIS CASSANDRA THINKS SO

The dollar's failure to strengthen in the wake of the latest rise in U.S. interest rates and the hike in the discount rate suggests that the Federal Reserve Board's ability to sustain the dollar may be waning, warns economist David Hale of Kemper Financial Services Inc. "Despite real short-term interest rates running about 4%," he says, "one has to wonder what will happen to the American dollar later this year if we are confronted with deteriorating trade and inflation news."

Hale notes that pessimism over the U.S. trade outlook is growing—not only because of the rise in oil prices but also because many experts think export growth will slow later this year in response to the dollar's strength in 1989. He also believes that the U.S. is likely to launch trade sanctions against Asian trading partners to force them to open up their markets to American goods—an action that would tend to raise inflation and frighten foreign investors in U.S. financial markets.

Finally, Hale predicts that inflationary foreign governments will continue to boost interest rates overseas, undercutting the support that U.S. rate hikes provide for the dollar. "The odds are growing that ebbing trade progress and the negative effect of an export slowdown on U.S. growth will precipitate a dollar crisis later this year."



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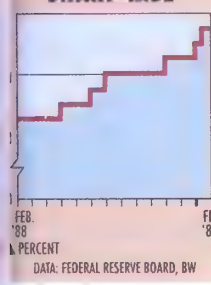
SAT INTERNATIONAL CONFERENCE CENTER

WILL THE FED'S TIGHTER GRIP ON CREDIT CHOK OFF THE EXPANSION?

The Federal Reserve Board is starting to play hardball. Responding to jumps in the producer and consumer price indexes for January, the Fed has hiked up short-term interest rates for the second time in two weeks. This assures the financial markets that the Fed is committed to holding inflation in check. But it raises new worries.

Higher rates make it more difficult to contain the S&L crisis. They make stock market investors queasy, because they dim the outlook for profits and lend a glow to the fixed-income market. And they impair the Administration's ability to tame the budget deficit.

THE PRIME RATE'S SHARP RISE



But more important, consumers will feel the bite of higher rates, and that could derail the expansion. Major banks boosted their prime rate again on Feb. 23, to 11.5%, lifting the cost of a broad range of consumer borrowing, from mortgages to car loans. That followed the jump to 11% on Feb. 10, from 10.5% (chart). From its low point in this expansion of 7.5%, the prime rate now has risen to its highest level since late 1984. The banks followed the Fed's lead. The central bank had lifted the federal funds rate—the interbank borrowing rate—by half a percentage point, to 9%. That followed a quarter-point rise only two weeks earlier. The federal funds rate has been the main tightening tool of the money managers during the past 10 months.

The Fed also hiked the discount rate—its borrowing charge to member banks—from 6.5% to 7%. Although the move had been widely anticipated because of the unusually wide spread between the discount rate and other short-term rates, it still underscored the Fed's intent on tighter credit.

CONFIDENCE HAS TAKEN A GIANT STEP

In coming weeks, the markets will again focus on the economy. Like the Fed, they'll be looking for signs that previous monetary tightening is taking hold. The central bank wants economic growth to slip into the 2.5%-to-3% range of its latest forecast.

But because recovery from the drought will boost 1989 growth by about half a percentage point, the range the Fed expects for the nonfarm economy is only 2% to 2.5%—and growth in the current quarter is clearly exceeding that pace.

A cooler economy requires slower growth in consumer

spending. Spending did slow in January, but other evidence shows that consumer fundamentals are solid.

The Conference Board's index of consumer confidence jumped 5.4% in February, to 122—the highest showing in more than 19 years (chart). Jobs are the reason. More than 34% of the respondents reported that jobs were plentiful, while only about 19% said jobs were hard to get. Those are the best readings in more than a decade.

In addition, income growth is healthy. Personal income surged 1.8% in January, to \$4,282 billion, the largest increase in more than a year.

A number of special factors influenced the January gain, the biggest of which was a surge in subsidy payments to farmers, after a large drop in December. But even excluding all of the onetime influences, the Commerce Dept. said that income still jumped 1.6% in January, following a 0.8% increase in December.

Wages and salaries, about three-fifths of income, accounted for most of the strong January performance. Wage income jumped 1.2%, the result of strong job growth, longer work hours, and rising wage rates.

CAR SALES WERE A DRAG ON SPENDING

The large income gain should keep consumers in a shopping mood, even though buying in the first quarter is off to a poor start. Consumer spending rose just 0.1% in January to an annual rate of \$3,352.6 billion, after increasing 0.8% in December.

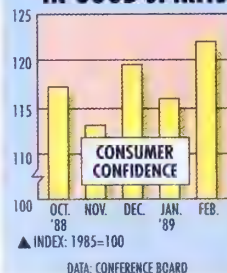
But the January weakness stemmed mainly from a 14.2% plunge in new-car purchases. Excluding autos, spending rose 0.6%. Purchases of nondurable goods advanced 0.9%, and services spending was up by 0.5%.

Unfortunately, all of January's spending rise came from higher prices. Inflation-adjusted spending fell 0.5%. That means real consumer spending started off the first quarter no higher than its fourth-quarter average.

The January weakness in spending is probably not an early sign that Fed tightening is taking hold, since income and confidence look so favorable. Also, car sales are down from a high December level. And with car lots overflowing, Detroit is sure to offer a new round of incentives, which could rekindle sales this spring.

The savings rate jumped to 5.8% in January from 4.3% in December. That, however, is largely an aberration in Commerce's numbers caused by the January slump in

CONSUMERS ARE IN GOOD SPIRITS



Business Outlook

car sales, rather than an indication of consumer caution.

Higher interest rates may be hitting housing, however. The Conference Board also reported that home-buying plans have weakened substantially in recent months.

CREDIT CAN'T PROP UP HOUSING

The Fed's tight grip on credit is a clear threat to the construction industry. Building activity already has hit its peak for this expansion. Construction contracting dipped last year, after climbing for five consecutive years. Housing kept the industry going in 1988, but with interest rates on the rise, building in 1989 could lose its major support.

Construction spending rose only 0.4% in January, to an annual rate of \$424 billion, even though the month's weather was unusually mild. And the value of new construction contracts, a leading indicator of building activity, fell 5% in January, to \$243.6 billion, according to the F. W. Dodge Div. of McGraw-Hill Information Services Co. The drop mainly reflected a big decline in the volatile public works sector, following a surge in December.

But the outlook is still dim. Residential contracting also fell in January, a sign that higher interest rates are depressing housing. So was the month's 7.4% drop in sales of existing homes. And going into March, mortgage rates had risen to their highest in 2½ years.

Contracting for business construction rose to its highest point since last August, but two large projects accounted for the jump. Industrial construction should stay strong since many industries are nearing their capacity limits, but the overbuilt office sector will remain weak.

INDUSTRY IS STILL ON SOLID FOOTING

The strength in industry shows up in manufacturers' order books. In January new orders for durable goods fell 3%, to \$128.1 billion, but that's no cause for alarm. Many hardgoods carry high price tags, which means orders can be volatile: Bookings had surged 7.3%

in December. Orders have risen 13.3% from a year ago and they remain in a firm uptrend.

Three-fourths of the January drop occurred in transportation equipment, mostly defense-related declines shipbuilding and tanks. Defense orders, less than 10% of the total, dropped 33.5%. Excluding that, durable-goods orders dipped only 0.4%.

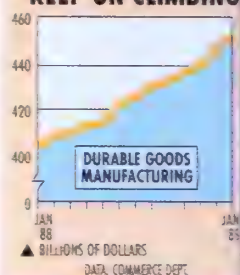
New orders for machinery and primary metals declined in January, as did demand for machine tools. The National Machine Tool Builder's Assn. reported that January orders plummeted 22.4% from last year's level with drops in both domestic and foreign bookings.

However, since tool orders in 1988 were the highest in eight years, the January drop probably reflects a fallback to a more sustainable rate of orders, not a slump in demand. New orders for nondefense capital goods—a leading indicator for equipment spending—rose a strong 1.5% in January.

In addition, hardgoods manufacturers already have plenty of work to keep them busy in coming months. The backlog of unfilled orders keeps expanding. In January it increased 0.9%, to \$451.7 billion (chart). During the past year the backlog has risen 11.6%. With their order books already bulging, producers have little reason to cut back output anytime soon.

The problem on the horizon, though, could be tighter Fed policy, since durable-goods manufacturing is such a credit-sensitive sector. Higher interest rates threaten cut into consumer demand for many big-ticket items. In particular, Detroit cannot afford weak car sales at a time when auto inventories are exceptionally high. That could mean production cuts. Higher rates also will cause companies to put capital spending projects on hold.

UNFILLED ORDERS KEEP ON CLIMBING



THE WEEK AHEAD

NAPM COMPOSITE INDEX

Monday, Mar. 7

The purchasing managers' index for February, compiled by the National Association of Purchasing Management, will most likely rebound to about 54.5% from January's low level of 53.2%. The NAPM surveys its members on changes in their companies' inventories, hiring, prices, delivery times, production, and orders. Although January's index was the lowest in almost two years, any reading above 50% indicates the economy is still expanding. In January the NAPM survey, which is skewed toward manufacturing, reported very small increases in employment and output—data very much at odds with government re-

ports. The February survey may pick up some of the strength missed in January.

INSTALLMENT CREDIT

Tuesday, Mar. 7

Consumer credit probably expanded by \$4 billion in January. Increases in revolving credit and personal bank loans were offset by a plunge in new auto loans. Installment credit in December grew by \$5.4 billion. Income growth has matched credit gains. Since mid-1987, the ratio of consumer debt outstanding to disposable income has leveled off at about 18.5%.

PAYROLL EMPLOYMENT

Friday, Mar. 10, 8:30 a.m.

The consensus is that nonfarm payroll employment grew by 275,000 in Febru-

ary. The dramatic jump of 408,000 new jobs in January was largely weather-related. The February numbers will probably erase the gain of 102,000 in construction employment posted in January. The expected overall February increase would be slightly more than the healthy average of 264,000 new workers hired each month in the last half of 1988.

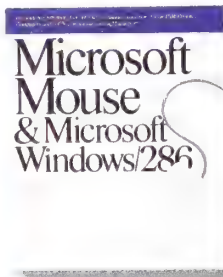
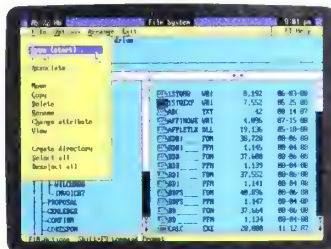
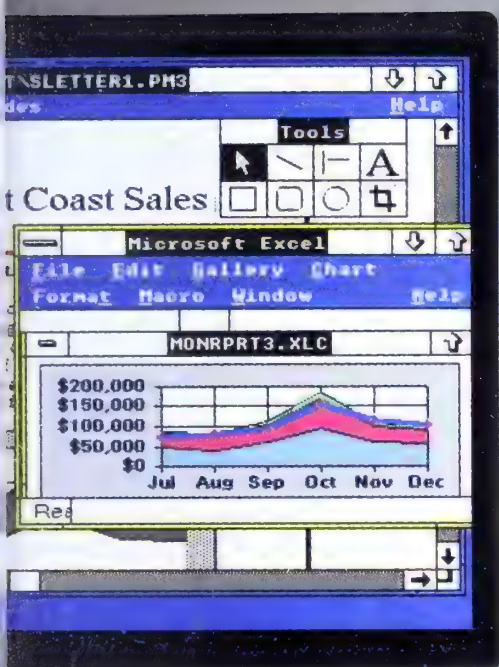
UNEMPLOYMENT RATE

Friday, Mar. 10, 8:30 a.m.

The expected increase in nonfarm payroll jobs suggests that the civilian unemployment rate edged down to 5.3% in February. The jobless rate was 5.4% in January and 5.3% in December. A February downtick will heighten concern about wage gains and faster inflation.

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TRYING TIMES AT BOEING

AS BUSINESS BOOMS, THE PRESSURES MOUNT

Is something wrong with Boeing Co.? The giant airplane manufacturer keeps getting in the news, and much of the news is bad. On Feb. 24 television around the world flashed images of a United Airlines Inc. Boeing 747 jet that had ripped open in flight early that day off Honolulu, killing nine passengers. It was the fourth fatal accident involving a Boeing jet since December. And the air disasters coincide with problems on the ground: Boeing's management, regarded as one of the best in the aerospace industry, has been badly embarrassed by recent quality-control problems and costly production delays of the brand-new 747-400.

Boeing is a victim of its own success. For 72 years the company has been building high-quality planes, and today, more than 30 years after it introduced its first jetliner, the Seattle-based giant commands 55% of the world's commercial jet market. So the odds are that a major plane accident will involve a Boeing-made aircraft, whether the company is at fault or not. And Boeing's market dominance seems assured through the 1990s, even in the face of fierce competition from McDonnell Douglas Corp. and Airbus Industrie. Just in late February, Boeing landed almost \$4 billion in new orders.

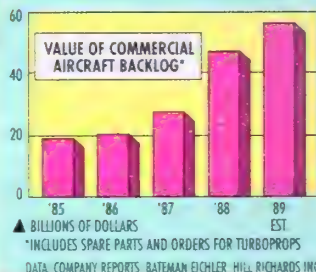
But the rush of new orders is leading to production demands the company is struggling to meet. The result: Boeing's sterling reputation for on-time delivery and top-flight quality has been tarnished. Says John Nance, an aviation safety expert based in Tacoma, Wash.: "People expect perfection from Boeing. When Boeing isn't perfect, everyone takes notice."

At the same time the company is feeling the effects of mounting public concern over air safety—even though investigators have not found the company responsible for a major accident since the 1985 crash of a Japan Air Lines 747 was directly linked to faulty repair work done by Boeing.

Boeing argues that it has been a leader in studying aging jets, and that most accidents stem from such factors as human error and weather, not airplane flaws (page



BOEING'S BACKLOG



BOEING'S BAD NEWS

- MARCH 1988** Japan Air Lines complains about quality of new planes. British Airways follows suit a month later
- APRIL 1988** An Aloha Airlines 737 loses part of its roof in midair, creating concern about older aircraft
- AUGUST 1988** The first in a series of miswirings in Boeing planes appears, raising questions about quality control
- JANUARY 1989** Boeing announces major delays in delivery of new 747-400s to a number of key customers
- FEBRUARY 1989** A massive hole opens in a United 747 flying over the Pacific. Nine passengers die

36). Nevertheless, the company is the target of intense, often hostile scrutiny around the world. The day after a recent Boeing 707 crash in the Azores, for example, a major Irish newspaper ran the taunting headline: "What has gone wrong this time, Mr. Boeing?"

'OVERCOMMITTED.' While Boeing grapples with the task of explaining its role in air safety, it must also handle some disgruntled customers. The company has piled up a \$50 billion backlog stretching into the mid-1990s (chart), and 1989 profits should jump 50%, to \$918 million, as revenues grow 29%, to \$22 billion. Profits should surge further as airlines start replacing aging fleets. Yet with production lines working overtime, Boeing has had to delay delivery of its first batch of 747-400s, the new version of its widebody, by two to six months.

That's the first time in 20 years Boeing has missed a delivery deadline.



FIG 747-400
R CONSTRUCTION

"We overcommitted," concedes Dean D. Thornton, president of Boeing's commercial airplane subsidiary. "We violated a covenant with our customers, and I'm pretty damn ashamed of it."

The company will be lucky if it can deliver the 57 new 747s it promised for this year. The push to meet the revised schedule will lower Boeing's profit margins on the 747 to 20%, down from the expected 25%, according to William N. Weatherage, an analyst at Dean Witter Reynolds Inc.

The delays, some announced on short notice, will force airlines such as KLM and Cathay Pacific to reschedule or cut back flights during the peak summer travel season, costing them millions of dollars in revenue. Even concessions at Boeing is now negotiating in an effort to appease its customers are little consolation. "We are angry," says Jürgen Weber, chief operations officer at

Lufthansa, which will not receive all six of the 747s it ordered for the year until December. "The whole fleet program will have to be reworked, but we can never fully close all the gaps this year."

Thornton, a 26-year company veteran who managed the successful 767 pro-

**'We violated a covenant
with our customers, and I'm
pretty damn ashamed'**

gram, now admits that Boeing underestimated the task of building the 747-400, which has 175 miles of wires and a few million parts. For one thing, the 747 cockpit required a total redesign to incorporate more advanced electronic controls and accommodate two crew mem-

bers instead of three. To give customers more choices, Boeing also attempted for the first time to win simultaneous Federal Aviation Administration certification for engines from three different manufacturers. And to satisfy unexpectedly heavy demand, the company doubled the production rate in just one year, which caused glitches in parts supplies and forced many planes to be assembled out of sequence.

'STRETCHED THIN.' That quickened pace is taking its toll on workers, too. Although employment at Boeing has jumped 83% since 1983, to 155,000, the increase in manpower has not been enough to relieve the pressure, especially since many of the new workers are unseasoned. Steven R. Huffman, a 747 mechanic, says he has worked 60 hours a week for the past 3½ years. "You're tired. There's no social life, no family," he says. "My wife would like to tell this place where to go." Admits Thornton: "We are stretched thin on resources."

Many in the industry wonder if the stress on workers will lead to quality slips. To counter that possibility, Boeing has stepped up training. At the Everett (Wash.) plant, 5,000 new workers have taken blueprint-reading classes and practiced riveting and drilling before starting assembly-line jobs. Boeing also conducts "pre-employment" training for serious job candidates at local vocational-technical schools.

Straightening out the 747 program is not Thornton's only manufacturing challenge. He also has to detect and correct any quality-control problems that remain. Several reported cases of miswiring on Boeing planes led to an unprecedented directive on Jan. 31 from the FAA ordering the inspection of most Boeing commercial planes produced since 1980. In all, 30 cases of miswiring and incorrectly installed plumbing were discovered. Most of them were in the fire extinguishing systems of cargo compartments.

The miswirings also provoked two sharply worded letters to Boeing from Leroy A. Keith, the FAA's top man in Seattle. Keith accused Boeing of waiting months before it reported miswiring on a Royal Brunei Airlines plane and told the company to review its entire approach to designing and installing components. Boeing's quality-control program is "not as good as it used to be," says Keith.

Boeing feels it violated no rules in reporting the Royal Brunei miswiring, but Thornton admits the company's design made it too easy to switch or incorrectly install the wires. He's already planning steps to make the system "Murphy-proof," and he says Boeing

is cooperating fully with the FAA's stepped-up surveillance of Boeing's production, inspection, and installation procedures.

As if all this weren't enough, Thornton and his managers have to worry about their competitors. A resurgent McDonnell Douglas has won an estimated \$9 billion in orders for its MD-11 long-range widebody. And Airbus Industrie will begin deliveries in 1990 of widebody A330 and A340 planes. "Boeing can't let

its guard down. Both its competitors will continue to challenge it on every front," says Howard Rubel, an analyst at C.J. Lawrence, Morgan Grenfell Inc. In a parry to the MD-11, Boeing expects to begin selling a derivative of its widebody 767, which will feature added seats and possibly a third engine.

Despite all its problems, Boeing enjoys the fundamental trust of its regulators and customers. "We do not question the safety of Boeing aircraft," says An-

thony Broderick, the FAA's associate administrator for aviation standards. Even Lufthansa's Weber, annoyed as he is, praises the company: "Boeing has built good aircraft in the past and will in the future." In the months and years to come, Boeing has to make sure it does not betray that trust.

By Maria Shao in Seattle, with Seth Payne in Washington, John Templeman in Bonn, Mark Maremont in London, and bureau reports

AVIATION

SURE, THE PLANE IS OLD —BUT IS IT DANGEROUS?

Airlines and regulators struggle with the problems of an aging fleet

The questions surrounding Boeing Co.'s production and quality-control problems are serious enough, but they're nowhere near as tough to answer as this: When is an old jet too old to fly safely?

There's no doubt that top-notch maintenance, including extensive repairs and parts replacements, can keep aging planes in the air for decades, with no appreciable risk to passengers and crew.

Yet it seems clear that at some point the balance shifts. The trouble is, no one really knows where.

In ways not dissimilar to the problems of decaying bridges and highways, America's air infrastructure is showing its age. The efforts will be gradually felt—in higher maintenance and inspection costs to carriers, greater concern among travelers over air safety, and growing pressure on regulators and builders to ensure that the jet fleet remains airworthy.

UNSUSPECTED FLAWS. The problem is particularly tricky because everyone involved is, in a sense, flying blind. Consider the Aloha Airlines incident last summer in which a heavily used, early model 737 lost part of its roof in flight. Boeing engineers who studied the incident were amazed to find that corrosion has a much bigger impact on aging aircraft than they had thought. Other such surprises seem likely, since it's a truism that you can't guard against a problem you don't know exists. Small wonder, then, that when a 19-year-old United Airlines 747 lost part of its fuselage off Hawaii on Feb. 24,

questions immediately focused on the plane's age—even though that

now doesn't seem to be the cause of the disaster.

Changes in the structure of the nation's air transportation will only make matters worse. Airplanes undergo their greatest stress during pressurization, and the hub-and-spoke operations spawned by deregulation mean shorter, more frequent flights. That, of course, sharply boosts the number of takeoffs and landings that each airplane makes in

a year—and shortens its useful life.

The obvious solution to the problem would simply be to arbitrarily ground the oldest and most heavily used planes in the nation's fleet, replacing them with shiny new jets. Yet even if that made economic sense—which is questionable—it's not an option. The world's airplane manufacturers simply haven't got the production capacity to meet such an increase in demand.

So all that's left are interim steps. One such move came on Feb. 28, when an airline industry task force recommended a massive overhaul of maintenance procedures for aging Boeing aircraft. The task force would make mandatory 20 procedures that currently are voluntary, including replacement rather than repair of critical safety parts and sections of the airplane skin. The report, which will

be followed by similar recommendations for other planemakers, "an effort to rebuild public confidence in older aircraft," says Paul A. Turk, an analyst with Avmar Inc., an airline consulting firm.

The task force's recommendations carry an estimated bill of \$800 million. That's not so bad since the outlays will be spread over a decade or more.

The carriers face other costs as a result of the growing concern over aging planes. Ray Valeik, Continental Airline Inc.'s senior vice-president of technical operations, says an earlier Federal Aviation Administration rule stemming from the Aloha accident forced the company to hire 150 additional workers. The carrier will replace 7,000 rivets in each of its Boeing 737s and may do the same for some 727s. Continental also needs to hire 150 more workers to make a variety of repairs and has had to add three planes to compensate for time spent on maintenance.

The aging skies of America are a problem everyone shares. And the solution will be neither quick nor cheap.

By Seth Payne in Washington with Todd Vogel in Houston



FATAL 747: GROUNDING ALL OLD PLANES ISN'T AN OPTION

LOOKING BACK WON'T TELL YOU WHERE PRICES ARE GOING

Hurry! Act now while supplies last! Prices are going up!

Echoes of the 1970s. The news was alarming enough: Consumer prices jumped at a 7% annual rate in January, and producer prices soared to a 12% clip. For a while after the numbers were released, it almost seemed as though a new inflationary psychology was about to take hold. Nervous investors dumped stocks and bonds, and economists warned darkly of the dangers of a wage-price spiral. Then, without much ado, the Federal Reserve Board tossed a bucket of cold water on the flames, raising the discount lending rate by half a percentage point, to 7%. That should cool things down, said some. Nope, not nearly enough water, said others.

Just how worried should you be about inflation? Moderately concerned, but certainly not panicky. Most economists agree that the January numbers were probably exaggerated. For one thing, food and fuel prices logged big gains after being relatively well-behaved for some months. Then there's what might be called the calendar effect. Many companies traditionally raise prices in January, and analysts say the seasonal adjustment applied to the raw numbers by government statisticians doesn't adequately take that into account.

Still, no one questions that there's been more upward pressure on prices recently. Excluding the volatile food and energy components, consumer prices grew at a 4.5% annual rate in the first three quarters of 1988. Since September the rate has leaped to 5.7%, says Stephen S. Roach, economist at Morgan Stanley & Co. Most economists agree that prices have moved into a higher growth track.

RIGHT SPIRAL. But that doesn't mean they're on an inexorable upward march, as they seemed to be in the 1970s. Back then, acute shortages of such key commodities as oil and wheat pushed their prices up several hundred percent. Those huge increases were subsequently "monetized" by a Fed that obligingly printed more money to help people pay the bigger bills. With more money in circulation, prices on all goods were bid up. That led workers to demand—and win—fat pay hikes, often in excess of inflation. Rising wages, in turn, stimulated demand fur-

ther—and begat still higher prices.

A weak Fed tried to unwind this wage-price spiral with small increases in interest rates. But they weren't enough because after inflation the cost of borrowing remained negative. Only after the Fed slammed on the brakes late in 1979 did the inflationary runup begin to subside.

Today's situation is far different. Cyclical pressures, not sudden shortfalls in supply, are nudging prices higher. The economy, now in its seventh year

est rates higher for several months.

What's not so clear is whether current Fed policy will suffice to keep inflation at bay. If it won't, the alternative is a dramatic tightening that could shove the economy into recession—a danger rendered all the more real by the fact that monetary policy doesn't work as quickly, or as precisely, as it used to.

Not so long ago, rising rates quickly choked off credit to the housing industry. Now rising rates simply make



of expansion, is running into resource constraints in certain industries and regions. And when strong demand bumps up against limited supplies, prices naturally move higher. Wages, meanwhile, remain largely in check—and should stay that way if the work force keeps expanding rapidly (page 90). Lawrence Chimarine, chairman of WEFA Group Inc. in Bala Cynwyd, Pa., notes that even the recent jump in unit-labor costs is more a reflection of declining productivity than rising wages.

But what's most different this time is that the Federal Reserve Board is on the case. In the early 1980s an energized Fed, with Paul A. Volcker at the helm, successfully wrestled inflation down. His successor, Alan Greenspan, may not appear quite so combative, but in word and deed he is no less an inflation-fighter. Growth in the broadly defined money supply, known as M2, has been sluggish for over a year, and the Fed has been nudging short-term inter-

est rates higher for several months. mortgages—many of them adjustable-rate—more expensive. So homeowners might meet steeper monthly payments by diverting discretionary funds away from stereos or a night at the movies. The effect on overall consumption would be slow to register. Indeed, consumer confidence remains at high levels, and personal income surged 1.8% in January.

The effect of Fed policy isn't the only uncertainty. Nobody knows just how strong the economy will be later this year, but forecasts are for an exceptionally strong first quarter, with a rebound from the drought helping to kick real growth up to a 5%-plus annual rate. Even if growth slows to 2.5% or so later, price pressures will remain, and that could drive rates higher. But don't expect a reprise of the 1970s. Today no one—not the markets, not investors, and not the Fed—is going to look the other way in the face of spiraling prices.

'CONGRESS HAS DONE IT TO US AGAIN'

To most taxpayers, filing isn't any simpler, fairer—or cheaper

Remember the great 1986 tax reform crusade? Its proponents promised a skeptical America that the revamped tax code would make filing taxes simpler, fairer—and for many, cheaper. But with another tax season upon us, BUSINESS WEEK interviewed harried taxpayers nationwide and found that most feel the reformers didn't deliver on their promises. As Greenville (S. C.) accountant Del L. Bradshaw puts it: "The general consensus is that Congress has done it to us again."

A national survey of taxpayers by accountants Ernst & Whinney confirms that view. Conducted late last year, the poll found that 44% favored the old system, only 36% liked the new law, and 20% were unsure. "People by and large are getting a little cynical," says E&W partner David Berenson.

It's not hard to see why. Washington has "reformed" taxes at a dizzying pace in the 1980s. In 1981, there was the Economic Recovery Tax Act, which slashed taxes by a record amount. The next year brought the Tax Equity & Fiscal Responsibility Act, which raised taxes by

the biggest amount up to that time. Two years later, Congress saw fit to pass the Deficit Reduction Act of 1984. Then in 1986 came the granddaddy of them all, the tax bill to end all tax bills. And don't forget the "technical corrections" laws passed in 1987 and again last year.



HOMEOWNER HIPPLE: HE FEARS NEW LIMITS ON MORTGAGE-INTEREST DEDUCTIONS

Now President Bush, despite his lips, is proposing to change the rules for capital gains and a host of other tax breaks. "It's more complicated now than it ever was," says Peter Kaufman, a tax lawyer in Needham, Mass. "It's like playing in a card game where they keep changing the rules after every hand."

True, Congress in the 1986 Tax Reform Act did perform a service by cutting rates, reducing the number of tax brackets, and sweeping away some notorious shelters. But it also irked taxpayers by abolishing a number of popular deductions. Consider Cleveland lawyer Daryl P. Rush. He earns upward of \$50,000 a year. But the virtual elimination of key business, medical, and interest deductions has hurt Rush, who used to depend on them for thousands of dollars in write-offs. Unmarried and with no dependents, he has few options left to cut his taxable income. The changes embedded in tax reform, Rush says, "place an undue burden on people of middle income."

The one remaining deduction available to most taxpayers is the seemingly sacrosanct family homestead. But J. R. Hipple, a Southern California public relations executive, is suspicious. In 1987, he and his wife Caroline, a sales manager for The End Up furniture stores, plunged into the white-hot Orange County real estate market. That's why they are concerned about the changes Congress placed in 1986 on the amount of mortgage interest deductible. While all interest is deductible on mortgages of less than \$1 million, Hipple worries that the interest limit is just a first step. "First they start with the rich guys," he says. "Then they'll say you can only write off \$25,000. Before long, it'll all be gone."

The Internal Revenue Service is studying

HOW THE IRS AIMS TO SIMPLIFY TAX PENALTIES

Uh-oh. The Internal Revenue Service just noticed that you "forgot" to declare \$2,500 in income on your 1987 tax return. How much will that oversight cost you?

Turns out such questions have no easy answers. But now—get this—the IRS is trying to help. While the service doesn't want to make life easier for taxpayers who stray, it does plan to clean up a crazy quilt of civil penalties that leave even income-tax experts con-

fused about potential punishments.

In the 35 years since the penalty system was created, ad hoc provisions have been tacked on as the tax cops have taken aim at one abuse or another. The 14 original penalties have grown to more than 150, and a simple error such as an overstated deduction may subject a taxpayer to a complex overvaluation charge, a 5% negligence penalty, and interest on the deficiency.

Both Congress and the IRS realize that overly harsh punishments might backfire and discourage compliance. On Feb. 21 the IRS recommended streamlining a number of its rules. Some of the suggestions:

- A simple, three-tier set of penalties for underpayments. Negligence or sub-

stantial understatement of income would be assessed at 20% of the deficiency. Gross negligence would incur 50% penalty, and fraud 100%.

- A similar penalty system for tax preparers. Fines would range from \$100 to \$500 per erroneous statement.

- A revision of fees against employer banks, and brokerages that fail to file W-2 and 1099 forms reporting income. Late filers now pay the same \$50-per-document fine as those that don't file.

Those ideas are only the IRS's opening bid in what could become a long debate over penalties. When the collectors and Congress get done, taxpayers will probably face a system that is much simpler, if not less painful.

By Catherine Yang in Washington



SH: TAX CODE CHANGES "PLACE AN UNDUE BURDEN ON PEOPLE OF MIDDLE INCOME"

the public's tax angst. Edward J. Seiler, assistant district director of the IRS office in St. Paul, Minn., says the agency would be thrilled to go for a year without changes in the law. "Let's get used to the system we've got," he urges. Seiler is sympathetic to taxpayers' complaints. The continuous tinkering "creates for us the same problems it does for them," he notes.

WART AND SWEET. So who out there is happy with the new tax law? Well, tax preparers are smiling. All the confusion driving hordes of new customers their way. Business is up 20% for accountant Adshaw. Meanwhile, at H&R Block Inc., based in Kansas City, Mo., the number of filings prepared jumped by 10% last year, compared with the usual annual increase of about 3%. Executive Vice-President Thomas M. Bloch even sees a glimmer of good news for taxpayers. For the first time ever, Block's average charge dropped last year—from \$41.41 to \$49.21. The reason? "Many people had shorter and simpler forms," Bloch says.

Does that mean tax reform is actually working out as billed? Bloch won't go that far. He acknowledges that most citizens have a rather jaundiced view of what constitutes a good tax system. "A lot of people judge their feeling toward the system based on the amount of their refund," he says.

Indeed, even though Bloch says refunds are up so far this year, taxpayer complaining continues. As the Boston Tea Party demonstrated more than 200 years ago, there's nothing like taxes to fire up Americans' emotions.

By Tim Smart in Washington, with an Foust in Atlanta, Maria Mallory in Ireland, Ronald Grover in Los Angeles, and bureau reports

HOUSING

ADULTS-ONLY HOUSING HEARS THE PITTER-PATTER OF LITTLE FEET

A new law limits age discrimination—and some seniors are in an uproar

Since last fall, Jamie Swartz has fought a condominium bureaucracy bent on evicting her. Her offense: being nine years old. That was too young for the "adults-only" Viewpointe Condominiums near Fort Lauderdale, Fla., where Jamie lived with her father and stepmother after Jamie's mother died of cancer. But on Mar. 12, a sweeping federal law banning housing discrimination against families and the handicapped takes effect, tilting the battle in Jamie's favor. "She gets to stay," says Viewpointe's attorney, Steven Weinberg.

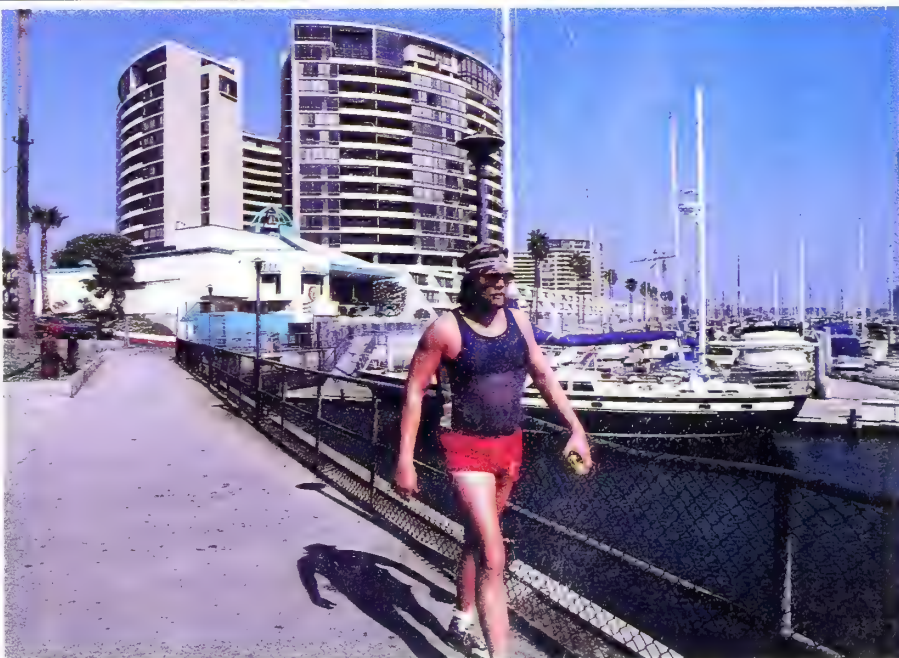
Jamie's dispute may be over, but the controversy over the new law is far from finished. Since President Reagan signed the extension of the Civil Rights Act of 1968 into law in September, the Housing & Urban Development Dept. has been bombarded with nearly 6,500 angry letters protesting the measure. Adults trying to steer clear of the youth

Lisa K. Mihaly, a staffer of the Washington-based Children's Defense Fund.

Real estate executives worry that the new law will drive up construction costs. It not only bars discrimination against families and the handicapped in multi-unit housing but also requires that new construction be accessible to the handicapped starting in March, 1991. Developers say that could boost construction costs by up to \$900 a unit, or around 2%.

GOOD INTENT. No one questions the law's goal: It aims to ease the shortage of affordable housing by opening up the 25% of the nation's rental housing stock that HUD estimates is now barred to children. Adding impetus to the drive was a dramatic rise in the number of homeless families, which now account for 30% of the country's homeless population.

Those concerns outweighed developers' complaints that the cost of building access ramps for the handicapped or fencing in swimming pools to protect



MARINA DEL REY: DESPITE A HIGH COURT ORDER, COMPLAINTS OF AGE DISCRIMINATION PERSIST

culture and its aura of noise and drugs complain that their property values will plummet if kids move in.

For the law's boosters, such fears have a sadly familiar ring. "I think it parallels what happened during the civil rights movement: concerns about who they had to rent to, who they had to let into their restaurants and hotels," says

kids would raise housing and rental prices. "What they're saying is that they'll deny somebody their basic civil rights because of a cost factor," says Representative Tony Coelho (D-Calif.). "There's a human side to this decision."

A few states have already had some experience with similar measures. California has instituted various age dis-

crimination bans since 1974, and an apartment complex in Marina del Rey was the subject of a landmark Supreme Court decision in 1982. The results so far have been mixed. Some 10% of that complex's 850 units are now occupied by families with children, but a nonprofit housing group still investigates more than 100 age discrimination complaints in Los Angeles each year.

The federal measure has some loopholes. It exempts communities whose residents are all over 62, or where at least 80% of the units are occupied by people over 55 and the development offers such services for the elderly as recreation areas and bus service.

WILLING TO PAY. Some adult communities will follow the path of Florida's Viewpointe condos and revise their policies. But others will try to qualify for the exemptions to gain adults-only status—and the premium seniors are willing to pay for it. "We're wary that the comfort and the serenity people enjoy here would be totally destroyed," says Edward A. Wegman, president of the board of directors for the 318-unit Hillsboro Cove Condominium in Deerfield Beach, Fla., which revised its policies in December to become an all-seniors complex.

Because of such efforts, critics say, the new law may inadvertently end up fostering some age discrimination. "It forces communities that wish to maintain their exemption to exclude individuals under age 55," says Gary Poliakov, a Fort Lauderdale attorney who represents about 400 adult-only communities.

Many adult communities won't qualify for the exemption: singles complexes and places that lack services for seniors. Mobile-home parks, which generally don't have such amenities, will be hit hard. "A lot of our people are seniors who have invested their life savings to live in a place with other adults," says Arlene F. Barnhart, vice-president of an 82,000-member mobile homeowners' group based in California. She worries that if mobile-home park managers spend money on new facilities to win an exemption, people on fixed incomes will face higher rents—or eviction.

Others think the law's goals were inevitable. "Florida has 1,000 people a day coming into the state, and unlike the past, a large portion of these people are families with children," says Alvin Waltzer, president of the Miami Board of Realtors. "We need places for younger people." In the end, the market could prove even more powerful than the new law in forcing people to mix with the Jamie Swartzes.

By Ron Stodghill II in Washington and Gail DeGeorge in Miami, with David Castellon in Los Angeles

STEEL

BOTH SIDES ARE GIRDED FOR GRUELING STEEL TALKS

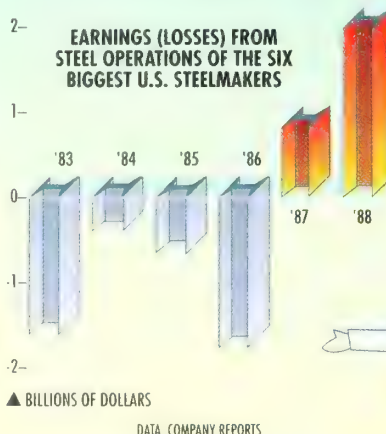
Workers feel big hikes are overdue—and companies are running scared

On the face of it, you might expect the steel talks set for this month between the United Steelworkers and four big steelmakers to go smoothly. While the union wants solid pay hikes after years of concessions, the greatly shrunken business is now more efficient than most countries' steel in-

we've gained the past few years, or competitors will pass us by," says one company negotiator.

That's not to say the companies afford to give something to the 450,000 workers covered by the expiring contracts. Since 1982, modernization and cost-cutting have helped boost produ-

STEELMAKERS ARE PROSPERING ONCE AGAIN...

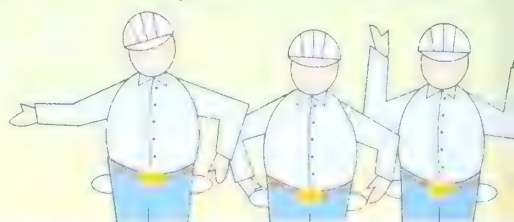


...BUT STEELWORKERS ARE STILL FEELING THE PINCH

	Average hourly earnings*		
	Dec., 1982	Oct., 1988	Increase
STEELWORKERS	\$14.40	\$14.76	2.5%
AUTO WORKERS	12.98	16.09	24.0
COAL MINERS	13.20	15.95	20.8
OIL WORKERS	13.49	16.49	22.2
CONSUMER PRICE INDEX			23.5

*Including overtime

DATA: UNITED STEELWORKERS



dustries. Booming demand has brought the companies \$3 billion in profits over the past two years (chart). So it all looks like a recipe for easy compromise.

It's not. While neither side expects a strike, the companies see danger lurking in a fat settlement. They worry that cheap foreign steel might pour into the U.S. again. Some executives also fear a renewed slump in demand later this year. And all four companies—Bethlehem Steel, Armco, National Steel, and Inland Steel Industries—are concerned about USX Corp., whose contract lasts until 1991. The No. 1 steelmaker could steal business if the others raise pay levels—and prices—too much. "We can't afford to lose any of the advantage

ity 6% a year, according to PaineWebb Inc. U.S. steel companies now use 10.5 hours of labor to make a metric ton of steel, vs. 7.1 hours in Japan and 6.5 in South Korea, PaineWebb adds. As a result, steelmakers have taken full advantage of renewed demand. Steel production climbed steadily in 1987 and 1988, the industry is running at nearly full capacity. And since 1984, when the Reagan Administration signed a voluntary export restraint pact with foreign producers, steel imports have fallen from 26.4% of the market to 20.3% last year.

TAKING ADVANTAGE. The specter of foreign competition isn't gone, however. Congress doesn't renew the import quotas in October, U.S. producers fear other countries might regain market share by increasing subsidies for their steel. U.S. companies could have a rough time meeting such competition if they're stuck with expensive contracts.

On the home front, USX is already trying to take advantage of the uncertainty brought on by the upcoming negotiations. Steelmakers say they see signs that steel buyers have been build-

'We're not looking to bankrupt any company. We just want our share'

their inventories against the possibility of a strike. And USX plans to woo customers with promises of steady supplies. Most jittery are steelmakers who depend on particular companies to buy a lot of their steel.

The USW, which has lost 197,000 jobs in a decade, knows the companies' problems. Fearing that even the threat of a work stoppage would cause buyers to seek alternative supplies, the union pushed to open negotiations early, even though the contracts don't expire until July 31. But members feel that it's time for a raise. Steelworkers' wages have climbed only 2.5% since 1982—below the inflation rate and far less than what union workers got in other heavy industries (table). "We're not looking to bankrupt any company," says Michael K. Lewelt, president of USW Local 1865 at Armco's Ashland (Ky.) plant. "We just want our share."

The union is likely to be influenced by the deal it won recently in aluminum. In December, aluminum makers agreed to wage and benefit hikes that could total more than 5% a year. But most of the increase will come in onetime payments, including profit-sharing and \$2,000-per-worker bonuses spread over the 43-month pact. The base wage will increase only 50¢ an hour. The terms of that settlement offer some consolation to the producers. The aluminum agreement is a little rich," says a steel company negotiator. "But it does show that the union is flexible in the way it will take more money."

DOUBLE PAY. Trouble is likely to start when industry negotiators demand productivity increases to offset wage hikes. Management intends to ask for workable changes, including multicraft agreements to allow maintenance workers to become "jacks of all trades." Some USW locals would probably resist such moves.

A still bigger fight looms over subcontracting. The union won major subcontracting restrictions in the last negotiations. But although the companies pulled subcontracted work back into their plants, they didn't hire more union workers. Instead, they increased overtime. In fact, the union estimates that the companies paid enough overtime in the past 10 years to create 15,000 new jobs. To counter this, the union plans to ask for a deal it won last month from car companies, who agreed to double pay, rather than time and a half, for employees who work more than 60 hours a week.

Both labor and management have been badly scarred by the shakeout of the 1980s, so neither side wants a bruising battle. The trick will be to come up with a contract that gives steelworkers more without making management feel at it has given away the store.

By Michael Schroeder in Pittsburgh

DEALS

GM'S ALPHABET STOCKS SPELLED TROUBLE

Did GM's deal with Hughes neglect the interests of other shareholders?

Alphabet soup isn't for everyone. Nor are so-called alphabet stocks such as GM's Class H and Class E shares. A Feb. 28 agreement between General Motors Corp. and Howard Hughes Medical Institute, rejiggering the deal in which GM bought Hughes Aircraft Co. from the institute in 1985, offers further evidence that this form of stock may be more trouble than it's worth—especially to outside investors.

The restructured deal patches up a dispute between GM and the institute. GM paid \$2.5 billion of the \$5.7 billion purchase price for Hughes Aircraft with 100 million newly created Class H common shares. It also gave GM stockholders one Class H share for each 20 shares of GM common they owned. The shares were designed to give holders a stake in what

the 99.5 million Class H shares it now holds, it could be left with a big loss if the share price tumbled after the guarantee expired Dec. 31. If it tried to sell even a portion of its holding before then, however, the sale would depress the price. GM would have to buy shares to prop up the stock or make up the difference later. Already, GM has supported Class H by repurchasing 3 million shares, and it plans to buy another 7 million.

'FINANCIAL COUP.' The restructured agreement calls for GM to swap \$975 million in cash and notes for 35 million of the institute's Class H shares. GM will no longer guarantee a \$30 price for all the institute's stock until Dec. 31, instead limiting the guarantee to 55 million shares at staggered intervals between 1991 and 1995. The institute plans to reduce its holding to 9.5 million shares, while GM's goal is to have 50 million shares in the open market by 1994.

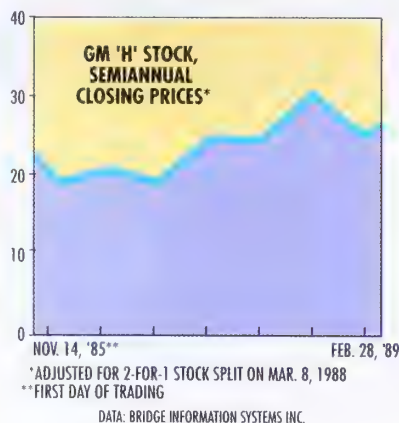
Both parties win. The institute will be able to diversify its portfolio gradually, while GM reduces its immediate potential liability in a way that stretches out its payments for Hughes. "For GM, it was a brilliant financial coup," marvels Peter Aseritis, an analyst at Smith, Barney, Harris Upham & Co. "They'll pay half up front and the other half over 10 years."

The news isn't as good for other Class H shareholders. Although the \$30 guarantee never applied to their shares, they had hoped that it would prompt more GM purchases. Trading recently at around 27¼, the Class H stock enjoyed a multiple of 13, compared with eight or nine for other defense-technology issues. But with the guarantee delayed until 1991, the stock price fell 1¼, to 26, in the two days after the restructured accord was announced.

Defenders say the new accord will prop up the price for an even longer period, while removing the threat of a sudden dumping of shares by the institute. Maybe so. For now, though, the resolution of the dispute favors the two parties at the negotiating table—perhaps over those who weren't invited. Here's the lesson, says Jack Modzelewski, an analyst at PaineWebber Inc.: "The average investor should just stay away from alphabet stocks."

By James B. Treece in Detroit

GM-HUGHES: GOING NOWHERE



would become GM Hughes Electronics Corp. Similarly, Class E shares were created in GM's takeover of Electronic Data Systems Corp.

The shares also came with a guarantee for the institute: If their open-market price fell below \$30 by the end of this year, GM would make up the difference, up to \$2 billion. Unlike Class E shares, though, trading in Class H shares remained thin: About 27.5 million shares are outstanding, excluding the stock held by the institute and GM. But fewer than a million shares changed hands on the New York Stock Exchange in 1988's fourth quarter.

As a result, the two sides were in a stalemate. If the institute didn't sell

INTEL TO MOTOROLA: RACE YA

The company's new 860 chip could leave its archrival in the dust

Intel Corp. marketing manager Kanwar Chadha is one guy who's willing to stand up for his company. Chadha was at the Feb. 27 unveiling of Intel's new 860 microprocessor when an engineer for Sun Microsystems Inc. voiced doubts over that chip's prospects in the computer workstation market. Chadha quickly offered him a \$100 bet: By the end of next year the top five workstation makers, including Sun, will have announced systems built around the 860.

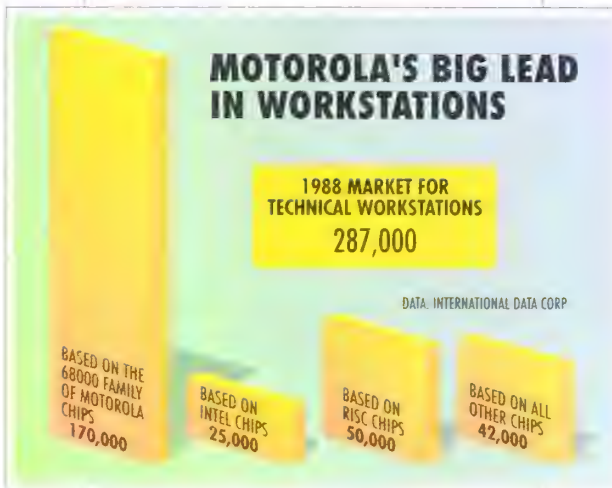
Intel has a lot more riding on the 860 than a C-note. The company's chips are now also-rans in the workstation market, the fastest-growing part of the computer industry. That market for computers used by engineers and designers rang up \$3 billion in sales last year. Market researcher Dataquest Inc. predicts it will top \$5 billion in 1990. If Intel snares all five customers, archrival Motorola Inc.—which supplies 60% of the microprocessors for workstations—could be the big loser.

James I. Magid, an analyst at Needham & Co., is also betting on Intel's superfast 860. The chip, he predicts, is "going to blow the other processors out of the market." Even Jack W. Browne, Motorola's director of microprocessor marketing, admits the new chip will propel Intel beyond its present stronghold in IBM-type personal computers. "Intel and Motorola are back in a head-to-head contest," he says. However, Browne insists that Intel's workstation gains will come mainly at the expense of upstart chips, such as those developed by Sun and MIPS Computer Systems Inc.

SPEED DEMONS. Others assert that Motorola is vulnerable because it undercut its own strengths last year by introducing a radically different chip to compete with those from Sun and others. This chip, called the 88000, features reduced instruction-set computing, or RISC. Trimming the menu of built-in instructions enables it to rip through almost 17 million instructions per second, twice as fast as Motorola's hottest conventional design. But the RISC approach sacrifices software compatibility. The 88000 won't run programs written for the older Motorola chip—the 68000—that won the

workstation market in the first place.

Thus, when a workstation company wants to upgrade to a faster microprocessing unit (MPU), there may be little incentive to stick with Motorola chips, especially if an MPU offering comparable performance can be had for less than the \$1,000 price of an 88000 chip set.



Apollo Computer, Digital Equipment, and Sun—the top three makers of workstations—are big 68000 buyers, but their high-end machines already have non-Motorola RISC chips. Offsetting those losses are some new customers, such as Data General Corp. and Stratus Computer Inc. So while defections "have been a

challenge," says Browne, "I wouldn't say they've been a problem."

With the advent of Intel's 860, though, defections could become a problem. Intel's chip boasts a RISC processor even faster than the 88000. In addition, the 860 has two other processors that are veritable speed demons when it comes to floating-point operations—calculations common to scientific problems and graphics processing. And the whole tripe-processor costs just \$750. A swifter model is due in September.

THE BRAINS. Intel's critics predict that the microprocessor king, long an opponent of RISC, will now find itself in the same quandary as Motorola. They say that its super-MPU shoots down Intel's next cash cow. This chip, called the 486, won't be launched until April to succeed Intel's fabulously successful 386, the brains of today's most powerful IBM-compatible PCs. Not to worry, say David L. House, general manager of Intel's MPU operations: When it comes to running IBM programs, the 486 will outdo everything, even the 860.

As for that \$100 bet, IBM, not among the top five workstation makers, is already working on Wizard, an 860-based "co-processor" card that will speed up its PS/2 personal computers, and there are reports of a full-blown workstation being in the works as well. There are hints that No. 1 Sun may also use the 860 as a co-processor.

Motorola won't take this lying down, of course. But Intel's 860 clearly has Motorola on the defensive.

By Otis Port in New York, with Richard Brandt in San Francisco and Lois Therien in Austin, Tex.

RESTRUCTURINGS

IF THE SHOE FITS, SELL IT?

Investors wonder why U.S. Shoe is unloading its most reliable earner

Philip G. Barach, chairman of U.S. Shoe Corp., has mystified onlookers for a long time. Competitors have wondered about his merchandising gaffes. And puzzled shareholders have had trouble figuring out exactly how he intends to turn around U.S. Shoe.

Now he's done it again by agreeing to sell the company's cash cow. How that's supposed to reward shareholders—other than through a promised dividend hike—is anyone's guess.

Barach spurred takeover talk in August when he announced he was exploring ways to give shareholders more bang for their buck. But instead of finding a buyer for the whole company, he opted on Feb. 27 to sell most of its footwear division to a group led by Merrill Lynch Capital Partners for \$422.5 million. In effect, he committed the company to its sickly women's apparel business and its smaller eyeglasses unit.

His decision to unload a source of st

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Assets \$2.2 billion
Revenues and Sales \$1.1 billion
Reported

Net Income \$125 million
Earnings Per Share \$2.91
*From Operations**

Net Income \$134 million
Earnings Per Share \$3.13
Dividend Rate \$1.72
Average Common

Shares Outstanding . . . 42.3 million
**Excludes One-Time Adjustments*

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ble, if unspectacular, earnings provoked a revolt on Wall Street. Shares of U.S. Shoe dropped 7¼, to 18, in the wake of the deal, the crowning blow to a stock that has dropped 31% since September. Barach now has to show a highly skeptical audience he's selling the right piece and can manage what's left.

WELL-HEELED CLIENTS. That's a tall order. U.S. Shoe's \$1 billion women's apparel business, which includes the Casual Corner, Ups 'N' Downs, and Caren Charles chains, has a dismal operating record. The retailers' troubles were largely responsible for the Cincinnati-

based company's 89% drop in third-quarter net income to \$1.3 million.

Barach says a turnaround is already under way. He predicts a 60% increase in fourth-quarter earnings. Over the past few months he has invested some \$225 million to expand distribution facilities, as well as to renovate and open new stores. He has also refocused 50 stores to target older, upscale women. Now it is up to his managers to follow through on his plans. But more than 20 top executives have left over the past two years.

He does have a few things going for

him. LensCrafters, the company's \$40 million eyeglasses business, has been on a tear. It has aggressively expanded into Canada and small U.S. towns. Outsiders say that LensCrafters' pretax operating income tripled in 1988, to more than \$3 million. "I like our niches. We're catering to the older customer," he says.

Clearly, Barach's strategy is to cash in on the graying of America. But while he's confident that the pieces are in place for a steady improvement, impatient shareholders may have other ideas that don't include him.

By Stephen Phillips in Cleveland

BANKRUPTCIES

NOW ALL GLOBAL MARINE NEEDS IS A MARKET

Chapter 11 put the driller in fighting trim, but oil prices still hurt

When Global Marine Inc. filed for bankruptcy in January, 1986, the offshore drilling market was fast taking on water. To save his company, Chairman C. Russell Luigs wrestled with one of the oil patch's biggest bankruptcies and juggled \$1.3 billion in debt. Oil prices continued to drop, the market was swamped, but still Global persevered. Now, after three bruising years, one of the largest drillers is starting anew. Global emerged from Chapter 11 on Feb. 28 with breathing room—for a while.

Global's reorganization leaves it among the strongest drillers. Luigs' massive spending on rigs during the early 1980s gave Global one of the industry's best fleets, and its capital costs have been cut in half, allowing it to make money with much lower rig rates. Meanwhile, many competitors, including Reading & Bates, Zapata, and Western Co. of North America, are still trying to find a lasting reorganization plan.

FOREIGN WORKERS. Still, Global's restructuring anticipates a rocky start. During the next three years the company has to pay only one year's interest, or \$45 million, on a still-massive debt of \$400 million. The remaining interest will be deferred. Other payments are tied to the profitability of its rigs. And the debt covenants don't require Global to turn a profit until 1993.

But even modern rigs make no money when they're idle. The industry still has nearly 200 unused

rigs, and only a handful of the working ones have long-term contracts. Rates for rig work have plunged from \$90,000 a day to \$23,000. All told, the situation is little better than 1986's depressed levels.

To cope, Luigs has cut the work force from a high of 3,047 in 1985 to 1,506 today. Overhead has plunged from \$59 million in 1984 to \$25 million today, and 86% of the rigs are staffed with lower-paid foreign workers. Global projects that it will lose an additional \$113.6 mil-

lion through 1992, when it hopes to turn its first profit in eight years. It lost \$155.6 million last year and a total of \$807 million since 1984. Still, Luigs is betting on the company's staying power. "Global will be the last man standing," he vows.

Global's second chance came at a steep price. Under the reorganization about 40 of its senior creditors received 90% of the company (table). They also have the right to add four board members to the existing 11. Subordinate debt holders received 7.5% of the stock. But Global's negative net worth of \$11 million nearly wiped out common and preferred shareholders: They received scant 2.5% of the company's stock, valued at around \$3.7 million, and warrants.

One group emerged nearly unscathed—management. Unlike those in many oil-patch bankruptcies, Global's executives kept their jobs. And they could wind up owning as much as 7% of the company if things turn out well. That may be fair, since a few people blame Luigs or the other Global managers for the company's travails. In 1978, as oil prices roared and speculators drilled feverishly, Global found itself with the oldest drilling fleet in the industry. Like everyone else, Luigs believed oil prices would continue to ratchet up, and he bet the ranch. He spent \$1 billion to transform a dilapidated fleet into the industry's largest and most efficient.

Luigs and Global Marine can do little more than bide their time waiting to see if that bet belatedly pays off. The company's fate still rides with the industry's, and more heavy weather in the oil market could easily sink three years' hard work.

By Todd Vogel in Houston

A FRESH START: DIVIDING UP GLOBAL MARINE

Group	Owed (millions of dollars)	Received
SECURED CREDITORS	\$700	\$95 million in cash \$400 million in debt 60% of the company
SENIOR UNSECURED CREDITORS	\$154	\$17 million in debt 30% of the company
SUBORDINATED BONDHOLDERS	\$400	7.5% of the company
PREFERRED SHAREHOLDERS	NA	0.7% of the company
COMMON SHAREHOLDERS	NA	1.8% of the company

TOTAL SHARES OUTSTANDING: 100 MILLION

DATA: GLOBAL MARINE INC.

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EDITED BY HARRIS COLLINGWOOD

DU PONT DOESN'T COTTON TO BLACKMAIL

► Last December an industrial spy delivered an ultimatum to Du Pont: Pay \$10 million, or competitors will learn the company's secrets for making Lycra, the popular fiber used in underwear, bathing suits, and other clothing. The chemical giant seemingly agreed to play along. But with the help of an undercover FBI agent, Swiss police nabbed the spy and three accomplices, all of them former Du Pont employees, as they tried to flee the Feb. 27 meeting in Geneva where they expected to receive their payoff. The ex-employees, who have not yet commented publicly on the charges, face up to 20 years in jail if convicted on charges of extortion and conspiracy.

The theft shows that even the most secure company can fall prey to determined insiders. A study done last year for the American Society for Industrial Security found that 48% of 150 companies queried had been similarly victimized.

A 24-YEAR-OLD TYCOON TUMBLES

► Things are getting rough for Michael Dell, the 24-year-old entrepreneur whose Dell Computer has become a major factor in the mail-order PC business. Slow sales of its IBM PC clones have left the company with \$105 million in inventory. So Dell is slashing prices by as much as \$1,500. Dell also announced that earnings for the company's fourth quarter, ended Mar. 1, will be 15¢ to 18¢ per share instead of the 25¢ to 30¢ that analysts expected.

ZENITH AND AT&T TEAM UP ON TV

► Zenith Electronics has decided that AT&T is the right choice. On Feb. 27 the last major American manufactur-

er of television sets teamed up with AT&T to develop high-definition television (HDTV) technology. Zenith will contribute expertise in TV design while AT&T will develop integrated circuits for an HDTV receiver. Bell Laboratories will work on digitally processing and transmitting high-definition signals.

The two companies have asked the federal Defense Advanced Research Projects Agency to kick in \$13 million to their three-year, \$24 million project. In a separate move, Zenith is seeking an additional \$10 million from DARPA for its \$21.5 million effort to convert its flat computer monitor into a high-definition TV screen.

RJR GOT BURNED ON HIGH-TECH CIGARETTES

► RJR Nabisco is extinguishing Premier, the high-tech, low-smoke cigarette unveiled with great fanfare in test markets late last year. Despite what analysts estimate was a \$325 million product development and marketing effort, the cigarette never attracted a core group of loyal consumers.

Premier's failure may dampen tobacco industry efforts to develop "cleaner" cigarettes that could extend the nicotine addictions of smokers. Philip Morris, which late last year hinted to BUSINESS WEEK it might unleash its own high-tech cigarette, now refuses comment about its

MAYBE HE SHOULD HAVE ORDERED A BUD LIGHT

Don't tell folks in the Dominican Republic about the thousand points of light. Facing a 1990 election, Joaquín Balaguer, the country's 82-year-old President, is trying to wow voters with a \$20 million lighthouse just outside the capital city of Santo Domingo. Dedicated to Christopher Columbus, the cruciform beacon stands nine stories high. What are supposed to be the explorer's bones will be buried at the foot, and a high-tech light system will beam the image of a cross 3,000 feet into the sky.

Trouble is, most Dominicans, who are lucky to get 10 hours of electricity a day, view the lighthouse as a beacon of folly. The aging generators that supply the island's electricity are crumbling, and a long-running contract dispute with General Electric has prevented a new generator from operating full time and solving the island's energy crisis.

Meanwhile, construction on the lighthouse is progressing nicely. On Jan. 30, the light system's first test run worked beautifully, beaming the image of a cross high into the clear night sky. The rest of Santo Domingo promptly blacked out.



new-product efforts. But RJR says it will continue searching for a viable product that caters to smokers' health concerns, most likely a variation of its Premier, which heated, rather than burned, tobacco.

EMPLOYERS CAN REPLACE STRIKERS

► In a major blow to organized labor, the Supreme Court ruled on Feb. 28 that striking workers are not legally entitled to get their jobs back once their positions have been filled by nonstrikers with less seniority. While the case technically applies only

to airline and railroad employers covered by the Railway Labor Act, lawyers say the broadly written opinion by Justice Sandra Day O'Connor could affect other private-sector employers.

The 6-3 opinion, which stemmed from a 1986 strike by TWA flight attendants, also gives an unexpected boost to the strike contingency plan of Eastern Air Lines, which intends to hire replacement workers if its machinists and two other unions carry out their strike threats.

LIZ CLAIBORNE'S NEW DESIGN FOR LIVING

► Liz Claiborne, 59, chairman and chief executive of the fashion design company she founded with her husband, Arthur Ortenberg, announced on Feb. 26 that she'll retire in June. Ortenberg, 62, will also retire. The couple, who will continue as directors, say they are quitting to pursue a number of environmental and social causes. Investors found their departure unfashionable: Liz Claiborne stock dropped more than a point on the news, to about 17.





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HOUSE DEMOCRATS BEGIN TO IMAGINE LIFE AFTER JIM WRIGHT

Some folks on Capitol Hill are beginning to think the unthinkable. Not since 1911, when Republicans dumped the tyrannical Joseph G. Cannon, has the House deposed Speaker. But the signs are mounting that Jim Wright (D-ex.) may be in deep trouble.

The House Ethics Committee has begun closed-door consideration of a staff probe into allegations of financial misconduct and the use of undue influence in support of savings and loan officials. The committee, which will issue a public report in mid-March, could recommend anything from no action to Wright's ouster from the House.

Ouster is unlikely, but even a call for a reprimand—the weakest disciplinary action available—could jeopardize Wright's future. That's because the Speaker's stock has never been lower. His sharply partisan and sometimes erratic running of the House has infuriated Republicans and often embarrassed Democrats. Wright badly damaged his own position by fumbling the proposed 51% pay increase for members and senior federal employees.

Odds are that Wright will weather the storm. Even the Republicans calling for his ouster see an advantage in having a wounded Speaker—especially at a time when Democrats are castigating the Bush Administration over ethics. "Wright projects an image that benefits Republicans," says former House Minority Whip Trent Lott (R-Miss.), now a senator.

THE LAST MAN. If the report triggers a rebellion against Wright, the beneficiary would almost certainly be Majority Leader Thomas S. Foley (D-Wash.). But Foley, who aides say is horrified even by speculation about his replacing the Speaker, would be the last man in the House to lead a coup.

If there is a move to dump Wright, a veteran House aide says, "it will start with a small group of Democrats holed up in a room somewhere." The key men to watch: Ways & Means Committee Chairman Dan Rostenkowski (D-Ill.), Energy &

Commerce Committee Chairman John D. Dingell (D-Mich.), and Representative Richard A. Gephardt (D-Mo.). Rostenkowski and Dingell have long dreamed of the top leadership job. Gephardt is a favorite of younger House members. But all three men have made enemies. And if Wright goes, Foley, whose position makes him the heir apparent, would probably end up as the consensus choice.

That's fitting, because Foley's rise through the House since being elected in 1964 has been less a matter of ambition than of being the right man in the right place at the right time. In 1974, Foley supported the conservative Bob Poage (D-Tex.) for reelection as Agriculture Committee chairman. But a rebellious Democratic caucus dumped Poage—and elected Foley in his place. In 1980 he was appointed majority whip. Upon the retirement of Speaker Thomas P. "Tip" O'Neill in 1986, Foley was unopposed for the No. 2 post.

Foley's politics put him squarely in the mainstream of his party. He has won a reputation as a consensus builder and a skilled parliamentarian. And he has kept his policy differences with Wright private. Foley doesn't share the Speaker's passion for soak-the-rich tax increases. A strong free-trader, he opposes legislation requiring foreign investors to register their U.S. holdings, a bill Wright is pushing hard.

But the style of a Foley House would be very different. The easygoing majority leader, whose mutt, Alice, has the run of the Capitol, is cautious to the point of sometimes seeming indecisive. "The guy has endless patience," says former House Counsel Stanley M. Brand.

At a time when congressional Democrats are adrift, it's not clear that Foley is what a party hungry for effective leadership needs. But Democrats, who dread the field day opponents will have dwelling on Wright's questionable actions, may just decide that it's time for the Speaker to move on.

By Douglas Harbrecht



FOLEY: A CAUTIOUS HEIR APPARENT

CAPITAL WRAPUP

THE ENVIRONMENT

William K. Reilly, head of the Environmental Protection Agency, is losing no time making his presence felt in the Bush Administration. For starters, Reilly is urging Transportation Secretary Samuel K. Skinner to order carmakers to achieve average fuel mileage of 27.5 miles per gallon in their 1990 fleets. The current standard is 26.5 mpg. The Reagan Administration had given carmakers another year to go the extra mile per gallon, but Skinner is reviewing the decision. Reilly says more efficient fuel use in automobiles "offers more potential pollution reduction than most of the

decisions that I am likely to make here." In other areas, Reilly says that while he favors voluntary compliance with government pollution standards, businesses should be prepared for a "reinvigorated" enforcement effort.

TAXES

Pro-family" tax bills are popping up like crocuses on Capitol Hill. The latest: A measure sponsored by Senator Orrin G. Hatch (R-Utah) that offers one-time deductions of up to \$5,000 for people who adopt children. Such bills may get a sympathetic hearing in the Finance Committee because Chairman Lloyd Bentsen (D-Tex.) is a champion of children's issues.

CAMPAIGN FINANCE

Inflation may be creeping up, but the cost of running for the Senate declined in 1988. Federal Election Commission figures show that Senate candidates spent a total of \$201 million, down from \$212 million in 1986. The drop appears to have more to do with geography than any change in campaign practices. Compared with 1986, last year's Senate contests included a larger number of less populous—and less expensive—states, such as North Dakota, Montana, and Wyoming. The cost of House races, though, continues to climb. Candidates spent \$257 million, up from \$239 million two years ago.



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THE POWER IS ON

GRAPPLING WITH THE GRAYING OF EUROPE

The Continent faces new social pressures as the ranks of youth shrink

In most places, the start of a new school year is cause for excitement—for children and parents alike. But in the village of Azat-Chatenet (pop. 168), nestled in the hills of the Creuse region in central France, the townspeople no longer celebrate *la rentrée*. In fact, the one-class grammar school is now shuttered for good. The reason? Aging inhabitants aren't producing any new students. "Forty years ago we had at least 30 children," says Mayor André Picot, a former pupil, now 67. "Last year we had four, so they made us close it. And we're not expecting any new kids."

From Mehamn in the far north of Norway to Ragusa at the southern tip of Sicily, it's the same story: Children are becoming rarer and old folk more numerous. As birthrates tumble and life spans lengthen (charts), Europe's population is aging fast. This graying of Europe is a time bomb that could explode into wrenching political, social, and economic turmoil.

Strains are already beginning to show. NATO's European conscript armies scramble to maintain strength as the number of potential draftees dwindles.

Government pension and welfare systems teeter on the brink of bankruptcy. Health care networks are stretched to the breaking point by the rising demands of the elderly. Across Europe, employers are desperate to recruit young workers as older ones retire. Baby-based industries, from toys to foods and diapers, face sharp contraction. That fate could spread to other, more crucial sectors—such as consumer electronics and housing—that depend on young singles and marrieds.

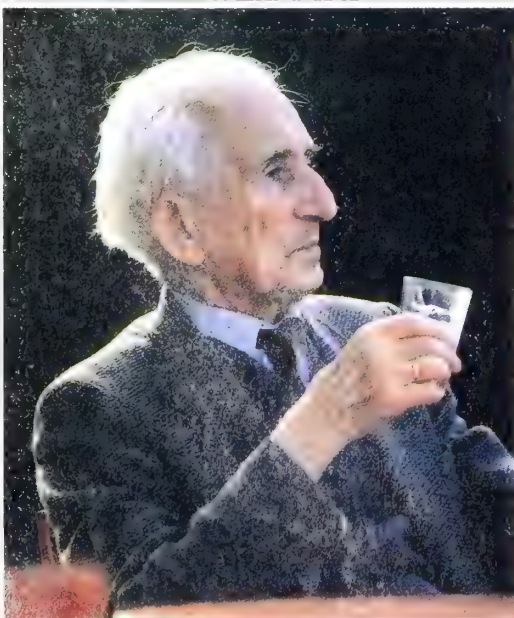
GENERATION GAP. The U.S. isn't far behind the curve, and Japan's population is aging fast, too. But the most dramatic change is in West Germany, where one person in seven is now under 15—down from one in four 20 years ago—and one in six is over 65. Western and Eastern Europe are headed the same way. Says Charlott Höhn, director of the Wiesbaden-based Federal Institute for Population Research: "No [European] country is ensuring its future population."

Indeed, the dramatic population trends raise questions about Europe's will to survive. "A society without young people is a society that dies," warns Jeanne

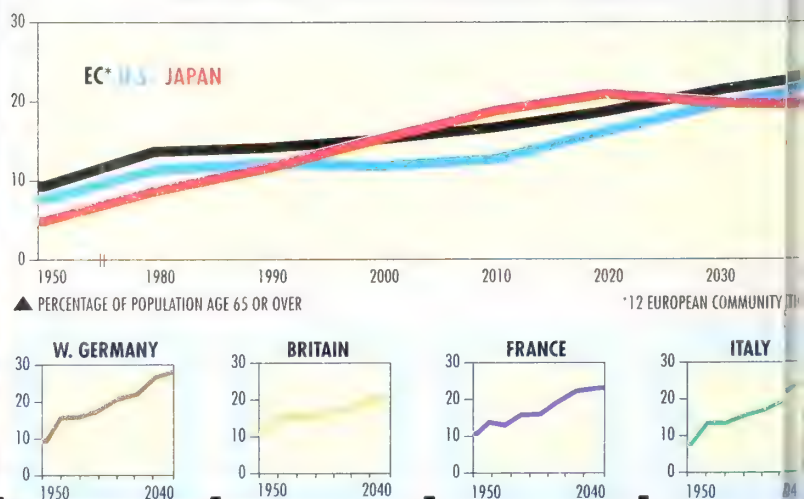
Fagnani, a sociologist at France's National Center for Scientific Research. National policymakers don't have easy answers to the complex problems raised by tumbling birthrates. That's because the problems stem from profound changes in the social fabric—from the new role of women in economic life to the availability of birth control and life-saving medical treatments to the demise of rural life. Yet if leaders don't begin to plan for the consequences, the shortage of resources could get worse.

One battleground will be between generations. Ballooning numbers of retirees, seeking a comfortable old age, could collide with the needs of shrinking numbers of workers who must pay the bills. The split of interests between generations could eventually rend whole societies apart. Such a skirmish broke out last year in Italy when the government moved to trim state pension rights. Three pensioners' unions quickly called out 250,000 protesters in Rome. The legislature had no choice but to give in.

Another battleground is between industrialized and underdeveloped countries. The U.N. estimates that only 50



AS EUROPE'S POPULATION AGES...



very 1,000 people added to the world's population in the next 20 years will be from industrial nations. That trend could heighten tension between rich countries and the Third World over markets, investments, jobs, and immigration.

Just how sharp these conflicts become depends on what impact aging populations have on economic growth. Some economists argue that the shrinking numbers of young people could slow growth as demand for goods and services dwindles. Others are more optimistic, arguing that it's the quality of the human resources available, not the quantity, that matters. This camp points to the high levels of training and education of postwar baby boomers.

ANITY. Opinions may differ over the economic consequences, but no one disputes the devastatingly simple arithmetic. Unless every 10 women in a society bear 21 children among them, populations inevitably shrink. Germany fell below this replacement level in 1970 and has since recorded 1.5 million more deaths than births. The population is expected to fall to 45 million or so in 2030, from 61 million now. "Germany is committing suicide," says Michel Levy, editor of the Paris-based *Population et Sociétés* magazine. The rest of Europe is hard on Germany's heels. If present trends persist, Europe's vaunted market of 320 million

people will peak in 2000 and fall to less than 300 million by 2040.

"We have to understand emotionally that we are becoming fewer," says Meinhard Miegel, executive director of Bonn's Institute for Economic & Social Research. "It will require a total change in outlook." Many business executives will have to update their concept of the oldsters' market. "The old, they feel, are set in their ways and don't spend much,"

ance companies collected over \$6 billion for retirement insurance in 1987," says Françoise Boitard, marketing manager for Assurance Générales de France. Italian retirees receive a substantial lump sum the year they stop work—the largest single dollop of discretionary income of their lives. They often blow it on such big-ticket consumer goods as new furniture or small homes.

Nor do today's oldsters shun vanity purchases. Cosmetics come high on their shopping lists, and companies are leaping into the market. Elizabeth Arden Ltd., the British cosmetics company, last spring launched a line of cosmetics called Millenium for the "mature" woman over 35. And in France, L'Oréal has developed several lines of anti-aging facial creams.

BIG PICTURE. Putting new twists on traditional consumer goods will be trickier. Auto maker Volkswagen is con-



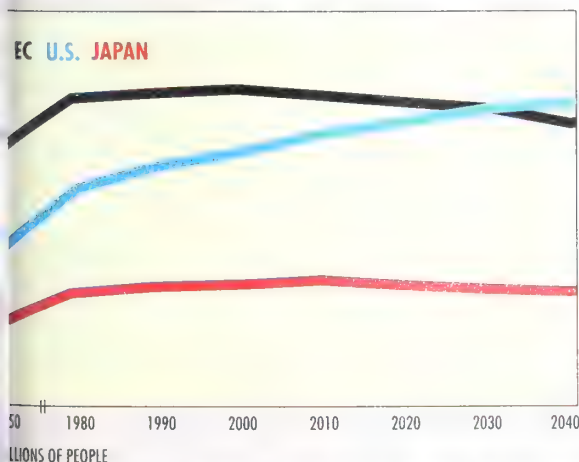
GERMAN FITNESS CENTER: THE ELDERLY REPRESENT AN AFFLUENT UNTAPPED MARKET

says Stephen Buck, research director at Audits of Great Britain, a market research outfit. In fact, today's elderly are affluent, active, and outgoing compared with their predecessors.

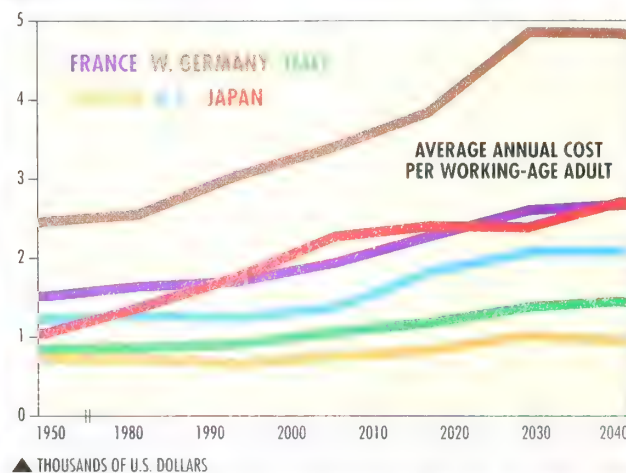
The over-55 population in Britain already holds two-thirds of the country's savings, making the elderly a dream market for financial services. In France, worries about the state pension scheme have spawned a booming new market that didn't exist seven years ago. "Insur-

sciously segmenting its markets by age. The company is targeting wealthy, older consumers for the German-made lines, while the Spanish unit concentrates on young customers for its cheaper models. Dutch electronics giant Philips has corporate planners brainstorming about how to tailor its businesses in consumer electronics, lighting, and medical equipment to graying markets. That includes making sophisticated consumer electronics goods such as VCRs and CD players

...AND BEGINS TO SHRINK...



...THE PENSION BURDEN GETS HEAVIER



with simpler instructions for the elderly.

As business thinks through these notions, it is getting conflicting analyses on the big-picture question: What impact will the aging population have on the economy? Those who look at the demand side of the equation are discouraged. Paul Johnson, an economist at London's Center for Economic Policy Research, warns that the costs of Europe's graying could "be far greater than the oil shocks of the 1970s and the recession that followed."

Those who look on the supply side see prosperity—in the short run at least—generated by postwar baby boomers who are more entrepreneurial and better trained than their parents. And they will have bigger amounts of capital to invest. In Germany alone, baby boomers will inherit more than \$54 billion in the next 10 years. The prospect of a venture-some generation with large sums to spend is reassuring. "Properly handled, a wave of corporate startups could be imminent in Germany," says Deutsche Bank chief economist Norbert Walter.

If he's right, Europe's graying might not be so painful. But in some countries, the labor force is already in retreat. Finland, for example, registered a decline of 0.5%, to 2.54 million, from 1985 to 1987. Other countries, such as France and Portugal, where numbers of workers are still rising slightly, have fewer men and more women in the labor force because of changing social behavior and the flattening population curve.

True, tighter labor markets produce more jobs for women. But the openings are a lure to the very same group, young marrieds, that governments are trying to persuade to stay home and have three children rather than one or two. Continuing low birth rates show that the mix of cash maternity grants and child-care payments common in many European countries doesn't work.

Tapping another source of population—immigrants—isn't working, either. Right-wing political parties vehemently opposed to immigration, such as Jean-Marie Le Pen's Front National in France, have won up to 14% of the vote in national elections. And such movements as Britain's National Front and Switzerland's Action Nationale also play on fears of race riots and the death of

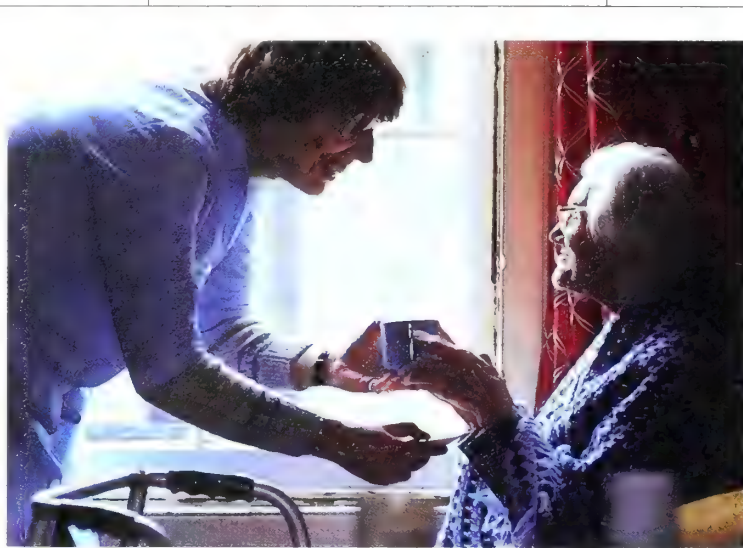
European culture to limit immigration.

For Germany, one source of new workers is "returnees"—persons of German descent allowed to leave Eastern Europe. About 100,000 flooded into Germany last year, more than double the 1970-87 annual average. Half the breadwinners already have industrial and technical skills. Munich-based carmaker BMW, for one, is considering using East bloc immigrants to replace increasingly scarce native workers. But even with a huge training budget to bring workers' skills up to snuff, BMW is battling for qualified people with other employers, such as electronics giant Siemens.

As the demographic vise tightens, such battles will become commonplace all over Europe. Britain's Industrial Soci-

ety to apply contributions immediately toward current pension payments. They worked in the 1960s and 1970s, when populations and economies were surging. Now, most funds are awash in red ink. Italy's national pension fund ran a \$895 million deficit in 1987 despite \$24.7 billion infusion. Together, European funds could be billions in the hole when future obligations come due.

The remedies, though, are political poison to any incumbent. Theoretically, contributions could rise. But in France, they already amount to half a typical worker's income—he pays 20% of his gross a deduction, with his employer paying 30% surcharge. Taxes could be used to bail out the funds. But in Germany, personal taxes are already as high as 56%



ELDERLY CARE IN BRITAIN: HOSPITAL COSTS ARE INFLATED FOR THOSE OVER 75

ety is warning local manufacturers that traditional sources of apprentices are quickly drying up. National Westminster Bank PLC is dangling a sign-up bonus of \$5,400 before prospective new employees in Britain's south. And labor unions have the same headaches. A 1989 study by the Cologne-based IW-German Economic Institute concluded that only 22% of today's workers under 25 years old joined unions, little more than half the 41% average for all German workers.

IN THE HOLE. Europe's military planners, too, face a numbers crunch. In Germany, Chancellor Helmut Kohl recently risked a political flap by extending the country's compulsory military service to 18 months from 15, starting in June. Otherwise, Germany might not be able to maintain the 206,000 conscripts needed to meet NATO commitments.

Social welfare systems are presenting politically explosive choices as well. Europe's government-run pension schemes are largely unfunded. Unlike in the U.S., the general European practice is

As governments seek spending cuts, some scary possibilities emerge. In Britain, hospital-care costs for those over 75 can be times the annual average for working-age adults. "I heard a suggestion at one conference that no life-preserving medical aid should be given anyone over the age of 75," says Eric Midwinter, director of London's Center for Policy Aging.

The picture is not gloom. The OECD figures that in such countries as Germany and Denmark, social spending could start to fall despite rising pension payouts. With fewer babies, the cost of infant welfare, family allowance payouts, and education will fall. If future labor shortages reduce Europe's chronic unemployment, the cost of benefits, too, will decline. The Confederation of German Employers' Associations figures payouts could drop \$100 billion in the next 20 years.

With ingenuity and imagination, European business and government could ease some of the transitional strains as Europe moves into a new era of aging and declining populations. But governments lack easy options and must solve inherently contradictory policy needs. Sorting out pensions and the welfare bind will be even harder. The toughest job of all may be reminding European voters that what appear to be the next century's problems are little more than 10 years away.

By John Templeman in Bonn, with Deborah C. Wise in Paris, Ellen Lask in Rome, Richard Evans in London, and bureau reports



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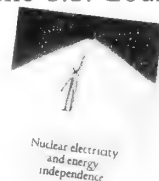
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HAS BUSH HELPED PAINT ROH INTO A CORNER?

Deset by rising unrest, now he faces new U.S. trade pressures

One reason President Bush added a snap five-hour South Korean visit to his Asian tour was to solidify relations with President Roh Tae Woo. The beleaguered Roh, in office for little more than a year, faces escalating labor unrest and student demonstrations, all tinged with anti-Americanism. Worse, he has promised to call a referendum on his performance soon—and he will have a tough time winning. Rather than lending a hand, however, Bush may have helped paint Roh into a corner by hitting hard at trade disputes.

Although dissidents and radical students called for nationwide demonstrations and Bush was forced to use a helicopter to avoid them, the broad middle class did not join in the protests. Bush also sent a positive signal by meeting key opposition leaders Kim Young Sam and Kim Dae Jung and promising to work together as equal partners. It was a clear attempt to ease fears that

the U. S. feels it can push Seoul around.

But the Bush Administration is getting tough on trade, and that is emerging as a key source of anti-Americanism. On Feb. 21 new U. S. Trade Representative Carla A. Hills designated Korea as one country that could face U. S. sanctions unless it lowers its barriers to U. S. telecommunications equipment. Korea's trade surplus with the U. S. fell from \$9.7 billion in 1987 to \$8.5 billion last year, but the improvement has not been fast enough to appease U. S. trade hawks.

CITRUS AND ALFALFA. When Bush arrived, he met Roh privately, and he is believed to have pressed for more rapid progress in opening Korea's markets to U. S. agricultural products ranging from beef to citrus to alfalfa. Then, in an address to the 299-member National Assembly, the President reminded lawmakers of Korea's responsibility in maintaining a fair trading system. As a result of

Bush's pressure, the government plans to notify the U. S. in the next few weeks what it will do to open its agricultural markets.

That will be tricky. Some 21% of Koreans are farmers, and they are angry because they feel bypassed by the country's rapid industrialization. Because Roh's Democratic Justice Party depends on rural support, his ability to maneuver on explosive agricultural issues is limited. "A large majority of Koreans have reservations about the U. S. because of trade pressures, particularly on opening of the agricultural market," says Lee Young-Ho, president of the influential Korea Policy Research Institute.

It won't take long to see just what the Bush effect will be. The next couple of months promise to be stormy. On Mar. 1 radical demonstrators led by the National Alliance for Democratic Movement tried unsuccessfully to march to Panmunjom, the truce village, to talk with North Korean officials. There are likely to be several more such confrontations with police. Student demonstrators are starting their spring offensive this month.

Wage negotiations also begin in March, and more factory lockouts are expected. As workers come under greater political influence from opposition politicians and dissidents, disputes are becoming increasingly violent, and lockouts are getting longer. At Hyundai



ANTI-GOVERNMENT DEMONSTRATORS: A RECENT POLL INDICATED ROH WOULD DO POORLY IN THE REFERENDUM HE HAS PROMISED TO CALL

Heavy Industries Co., for example, the continuing battle between moderate and radical factions has resulted in hundreds of injuries and hundreds of millions of dollars' worth of production losses.

With Korean companies already burdened by appreciation of the won, increased wages, and higher raw materials prices, they are unlikely to give in easily to labor demands. The Federation of Korean Trade Unions wants an average wage increase of 26% this year. But the Korea Employers' Assn. is offering only 10% and is expected to take a hard-line position. A nationwide strike is likely this summer.

At some point, Roh must submit to the "assessment" he promised Koreans prior to the September, 1988, Olympics. The latest betting is that he will call some form of referendum in mid-April. But in a nationwide poll conducted on Feb. 22 by the *Chung Ang Ilbo* newspaper, as many as 40% of those polled rated Roh below 5 on a scale of 1-10. Many ordinary Koreans are unhappy with Roh because prices for consumer goods have shot up nearly 10% during his first year in office. Even some elements of the normally pro-government business community are disappointed with Roh for giving in too easily to U.S. trade pres-

sure. If he were to lose a referendum, would spark a deep political crisis.

Roh has been hobbled in dealing with his myriad challenges by a protracted series of National Assembly hearings of the corruption and brutality of his former mentor and predecessor, Chun Doo Hwan. Roh is pressing for an end to the hearings, but the opposition is unlikely to accede without a firm commitment from Roh to call Chun to testify. Roh is not expected to oblige. With Roh skating close to the brink, too much shoving by the Bush Administration could push the President right over.

By Laxmi Nakarmi in Seoul

WEST GERMANY

IS THE GERMAN FEATHERBED ON ITS WAY OUT?

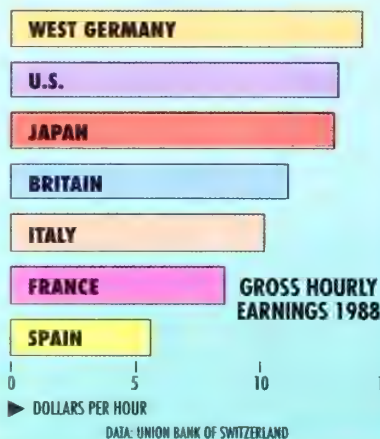
Labor's fat pay and short hours may not survive the rigors of 1992

West German printing companies must go to extraordinary lengths to get a job done on a weekend. When Aachen-based printer Helmut Achilles receives rush orders late in the week, he ships them to a French partner so he can meet Monday delivery deadlines. The reason: Union contracts in Germany keep printing companies, except daily newspapers, shuttered on Saturday and Sunday.

Now the printers and other unionized companies across Germany are going to the mat with unions over weekend work and other restrictions. The companies want the unions to adopt more flexible work practices before Europe moves toward a unified market in 1992. The printers are the test case. On Feb. 24 collective-bargaining talks between employers and the 165,000-member IG Druck printers' union stalled over the employers' demand for an end to the longtime ban on Saturday work. As warning strikes erupted, union leaders edged toward the first major walkout in Germany since 1984. The standoff could presage a wave of labor conflict as other industries gear up for tougher competition.

NO LATE HOURS. Labor agreements covering half of Germany's work force expire next year. Among the most important: the contract with the powerful IG Metall steelworkers' union, which paralyzed Germany's auto industry when it walked out five years ago. IG Metall wants to cut the workweek by 1.5 hours to 35 hours, while winning higher pay. But union chief Franz Stankühler vows that IG Metall will refuse to agree to Saturday work as a compromise. Mean-

FAT PAYCHECKS FOR GERMAN WORKERS



while, HBV, Germany's retail, banking, and insurance union, plans to turn down weekend work in its collective-bargaining negotiations this year. It has already snubbed employers' demands to allow service businesses to stay open later than 6:30 p.m. one evening a week.

These clashes point to a marked change in Germany's labor climate. The country has enjoyed greater labor peace than its European neighbors, thanks partly to postwar cooperation between unions and employers to rebuild the economy. But having gained so much, including some of the world's highest wages (chart) and shortest working hours, German unions fear they have more to lose in a post-1992 Europe.

Union leaders are increasingly intrans-

igent because they fear that if they give an inch, a mile of concessions will follow. Says Hermann Zoller, an IG Druck spokesman: "If we lose, it will have a negative impact on other industries." Union officials claim that German industry is merely using the threat of 1992 to wrest back hard-won gains. "1992 is the black cloud employers paint on the sky," says Alfred Lindeken, an IG Druck member and chairman of the workers council at Axel Springer Press. "It isn't that grave a change."

But the unions' inflexible stance may backfire. If IG Druck refuses to loosen the Saturday work restrictions, Achilles says that he may move his \$14 million company, Druckhaus Achilles, to Belgium, France, or the Netherlands, where work rules are easier. Other companies echo that threat. "Strategically, we have to find a location outside Germany," says Jochen Frangen, a board member at Gruner & Jahr, a Hamburg publishing house with \$1.7 billion in sales. **NO COMPROMISE?** Lower production costs and more flexible work rules already have lured Volkswagen to plant investments of \$5.8 billion in its Spanish unit, SEAT, over the next 10 years. The auto maker announced in late February that it wants to boost production in Spain by 33% by 1994.

If they want to achieve their overall goals of a 35-hour workweek and higher wages, German unions will have to modify their rigid stance over the next three years. Even some leaders of the labor-friendly Social Democratic Party (SPD) want the unions to give in. SPD Deputy Chairman Oskar Lafontaine, for example, stunned unions last year by backing weekend production to achieve shorter hours. His latest idea: a three-day workweek in exchange for allowing machines to run 24 hours a day, including weekends. Although German unions are loath to admit it, they will either have to be equally creative or end up fighting for a lost cause.

By Gail Schares in Bonn

HE MAY NOT BE COVERED PROPERLY.



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FRANCE

THE CHEVALIER BLANC HEADING THE INDUSTRY MINISTRY

Roger Fauroux's mission: To keep raiders away from French business

As chairman of French industrial giant Saint Gobain, Roger Fauroux won praise for acquisitions that made the company a heavyweight global competitor. Now, Fauroux is the powerful Industry Minister in France's Socialist government, and he finds himself on the other side of the mergers-and-acquisitions fence.

Fauroux, 62, is the Socialists' point man in France's new attempt at forging an industrial policy. His mission is to ensure that French industry pulls through the coming restructurings as Europe moves toward a unified market in 1992. Preventing raiders from picking off France's top companies is the key. Says Fauroux: "France needs strong global companies that rank in the top three in world competition."

Talk of curbing takeovers already is setting off warning lights. Says René de Laportalière, director of Libertés Services, a free-market lobby group: "It's French interventionism in another form, an attempt to bypass the market." Meanwhile, says acquisition trackers PF Publications, French companies spent \$20 billion outside France on acquisitions, twice what outsiders spent in France in 1988. "The French are playing a risky game," says a British EC official. "If you circle the wagons, you're open to retaliation."

SLEEPING GIANT. Fears of merger mania run deep. After recent stock market scandals, French President François Mitterrand went on television and denounced raiders as "financial gangsters." His point: that fast money on the Bourse had corrupted even his own officials. Some French companies are lobbying the government to set up a \$1.7 billion fund to protect the "national industrial heritage" by taking stakes in threatened companies.

The Socialists fear that such French blue chips as Club Méditerranée or food

giant BSN will be snapped up by cash-rich European players such as West Germany's Siemens or British financial companies—not to mention U.S. and Japanese interests. Above all, says Fauroux, "we want to prevent purely financial or speculative raids that you see in the U.S. or Britain."

A Germanophile, Fauroux is looking across the Rhine for ideas. The French are attracted by the German merchant banks, which hold large blocks of industrial stocks and have shut out raiders. In



FAUROUX: HOLDING UP TAKEOVER BIDS WHILE URGING "FRENCH SOLUTIONS"

France, that financial firepower belongs to the government. It controls the largest banks, insurance companies, and other financial-services concerns, with assets of close to \$1 trillion.

The sleeping giant is the state-controlled Caisse des Dépôts, with \$250 billion in savings deposits and managed funds. As a test run, it took part in last fall's government-backed raid on commercial bank Société Générale. Another potential white knight is Union des Assurances de Paris, an insurance giant. Led by Fauroux's friend Jean Peyrelevade and with \$22 billion in managed assets, it's eager to play the defender role. Says Fauroux: "We have to rechannel that money to French companies."

While Fauroux insists that govern-

ment policies are not directed against foreigners, some U.S. companies are feeling the heat. Hoping for a "French solution," the Socialists are holding up a \$300 million bid by International Paper Co. for French papermaker Ausseada Rey, announced on Jan. 12. In late February, French papermaker Arjomar Prioux finally put together financing to make a counter-offer. Similarly, a \$16 million bid by 3M Co. last fall to buy French spongemaker Spontex is being challenged by a consortium that includes investment bank Compagnie Financière de Suez and a local management-buyout fund. No decision has been made, but the Americans stand to face similar challenges on future deals.

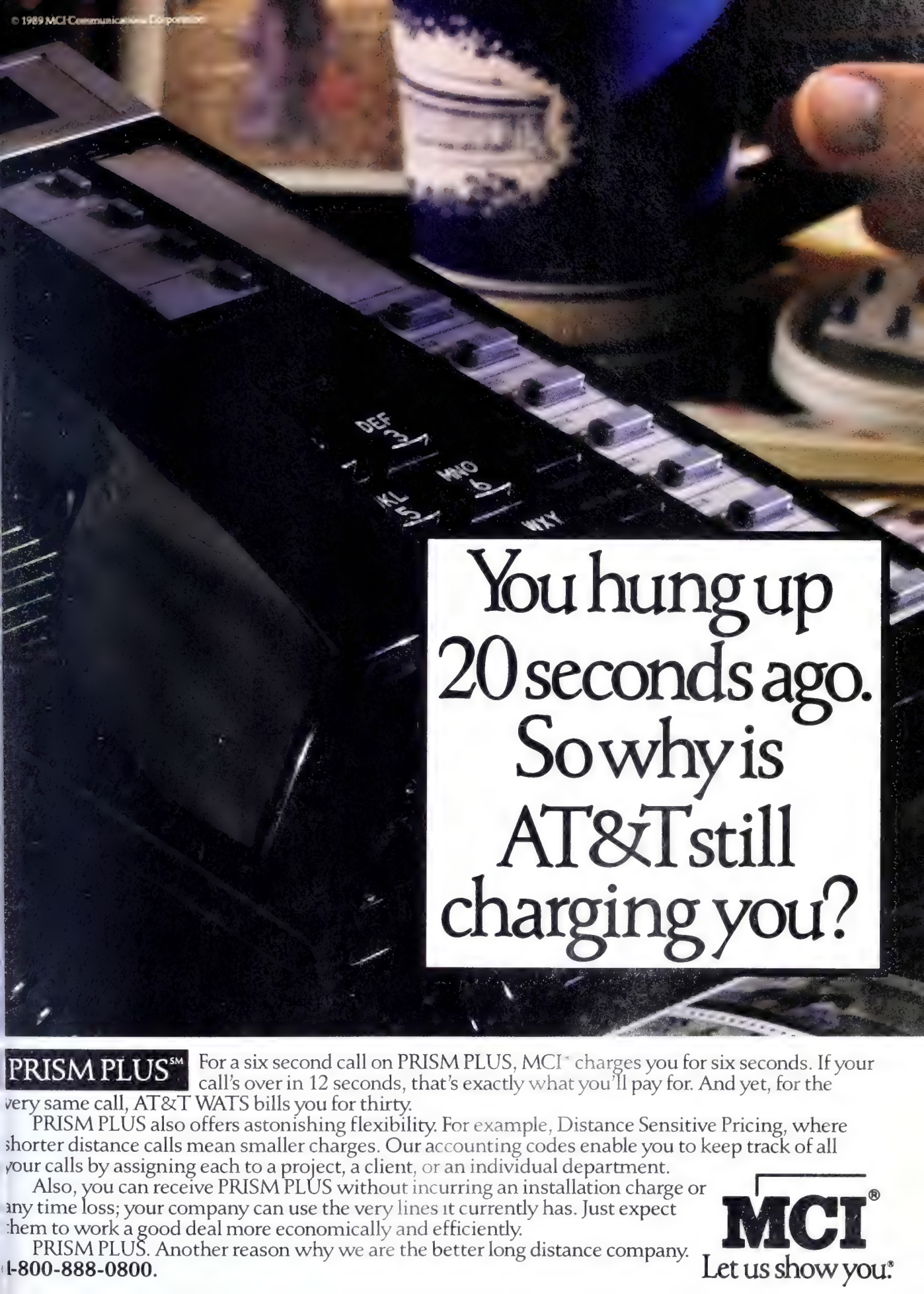
NEWCOMER. While Fauroux wants to defend French industry, he's likely to be more pragmatic than the economic nationalists who held his spot in the past. His 25-year career at Saint Gobain

which ended in 1986, included such major overseas drives as the purchase of U.S. building supplier CertainTeed Corp. His interests are wide-ranging. He founded the elite Fondation Saint Simon, which put Left Bank intellectuals in contact with business and political leaders and holds a degree in theology. Says current Saint Gobain Chairman Jean-Louis Beffa: "He is an intellectual but also likes the action business."

Still, as a newcomer to high politics, Fauroux's lack of political savvy nearly cost him his job. While the Socialists were catching flack as an insider-trading scandal swirled around Pechiney's recent acquisition of Triangle Industries Inc., Fauroux bluntly told a French journalist that he should dig into a far bigger scandal involving the Finance Ministry-led raid on Société Générale. Enraged, Finance Minister Pierre Bérégovoy demanded Fauroux's head. Fauroux's longtime friend, Prime Minister Michel Rocard, saved him.

Despite that run-in, Fauroux is making his debut at the polls. In March he's running for mayor in Giron, his hometown of 9,000 in the French Pyrenees. While he claims to be an independent, he's running on the Socialist-backed ticket. One way or another, the former CO is learning politics in a hurry.

By Frank J. Comes in Paris



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SOUTH AFRICA: A STEP FORWARD ON NAMIBIA, A STEP BACKWARD AT HOME?

Under State President Pieter W. Botha, South Africa's governing National Party (NP) has maintained white rule and kept itself in power with a gradual reform strategy: easing apartheid, but at a tortoise-like pace. Continuing that cautious formula may be harder for Frederik W. de Klerk, who became the party leader last month after Botha suffered a stroke. De Klerk, a conservative who now serves as Education Minister, is also likely to succeed Botha as President. But he faces mounting economic troubles and deepening political divisions, both inside and outside the party.

De Klerk and other party leaders want the weakened Botha to call a national election as early as May to consolidate the NP majority in Parliament before such problems erode the party's support among voters. They also want Botha to step down as President after the elections, clearing the way for de Klerk to be picked to succeed him by an electoral college dominated by NP members of Parliament. But de Klerk's political base could be weakened if white voters narrow the NP's majority by turning to the right-wing Conservative Party—as they did in municipal elections last fall, particularly in de Klerk's political stronghold in Transvaal province. If that happens, the NP's moderate wing may push a rival presidential bid by 49-year-old Finance Minister Barend J. du Plessis, who ran a close contest against de Klerk in voting for the party leadership on Feb. 2. Du Plessis' followers think the NP must move faster than in the past toward accommodation with blacks or be overwhelmed by South Africa's troubles.

'PETTY APARTHEID.' This year, Pretoria has little choice but to take a series of difficult steps that will risk alienating conservative whites. To prepare for talks with foreign creditors on the nation's \$11 billion in short-term debt, the government will have to brake the already sluggish economy. And to ease Western antiapartheid pressures, including economic sanc-

tions, Pretoria may decide to free imprisoned African National Congress leader Nelson Mandela. But that could trigger more black political unrest—and a white political backlash.

Last fall a swing to the right gave Conservatives control more than half of South Africa's white town councils. So they have reimposed restrictions against blacks' use of parks and other facilities that had been desegregated by NP-dominated councils. But to retaliate against this "petty apartheid," blacks

are boycotting white businesses. If boycotts succeed, they could help the NP by showing white voters that hardline Conservative tactics are unworkable.

For NP strategists, a major incentive for holding elections soon is to minimize the short-term political damage from Pretoria's decision to give neighboring Namibia its independence. Charges against right-wing South Africans of a "sellout" are likely to intensify next November when the leftist South West Africa People's Organization (SWAPO) is expected

to win Namibia's first election. But longer-term, South Africa and the NP government should reap important benefits from freeing Namibia. The independence accord eases South Africa's diplomatic isolation and ends the financial drain of administering the colony and fighting SWAPO guerrillas.

Diamond giant De Beers Consolidated Mines Ltd., which sent top executives to London recently to confer with SWAPO leader Sam Nujoma, and other South African mining companies foresee business as usual in Namibia, although they may have to pay higher taxes and deal with stronger unions. Because of Namibia's continuing economic dependence, SWAPO officials concede that they will need to maintain working relations with Pretoria. While the NP's cautious approach to reforming South Africa may be overtaken by rising political pressures, Namibia's bolder move to grant independence may allow Pretoria to continue playing an influential role.

By Alan Fine in Johannesburg



SOME PARKS HAVE BEEN RESEGREGATED

GLOBAL WRAPUP

SPAIN

The collapse of an ambitious plan to merge Spain's two biggest privately owned banks has seriously set back Prime Minister Felipe González' push to reform the country's inefficient financial system in time for the deregulation of European markets in 1992. Banco Español de Crédito and Banco Central together would have formed one of Southern Europe's largest banking groups. The deal fell apart because of infighting among the banks' officials and a much-publicized sex scandal involving main shareholders.

The misfire adds to the political pressures on González, who had staked his

prestige on the merger. His government was already on the defensive after a break with trade unions that triggered a general strike on Dec. 14. Stalled negotiations over pay and unemployment benefits, along with rising inflation, could take more of the luster off Europe's briskest economic boom.

JORDAN

A deepening economic crisis in Jordan is causing serious hardship for Palestinians, already squeezed by the economic disruption that their uprising has caused in the West Bank and Gaza. Jordan's dinar has fallen to \$1.90, down nearly 40% in the past year, partly because of declining aid

from Arab oil states and lower remittances from Jordanian workers abroad.

Palestinians in the West Bank and Gaza have been hit a double blow. The buying power of salaries paid in dinars has fallen sharply, and the value of savings, which many held in dinars, has shrunk. Jordanian curbs on produce imports have cut farmers' income from their main market, and the Israelis, making matters worse, have stepped up tax collections.

Some Palestinian economists say the crisis may intensify the uprising if unemployment rises and people feel they have little to lose. But Israeli military observers say the economic pressure of recent weeks has reduced the unrest.

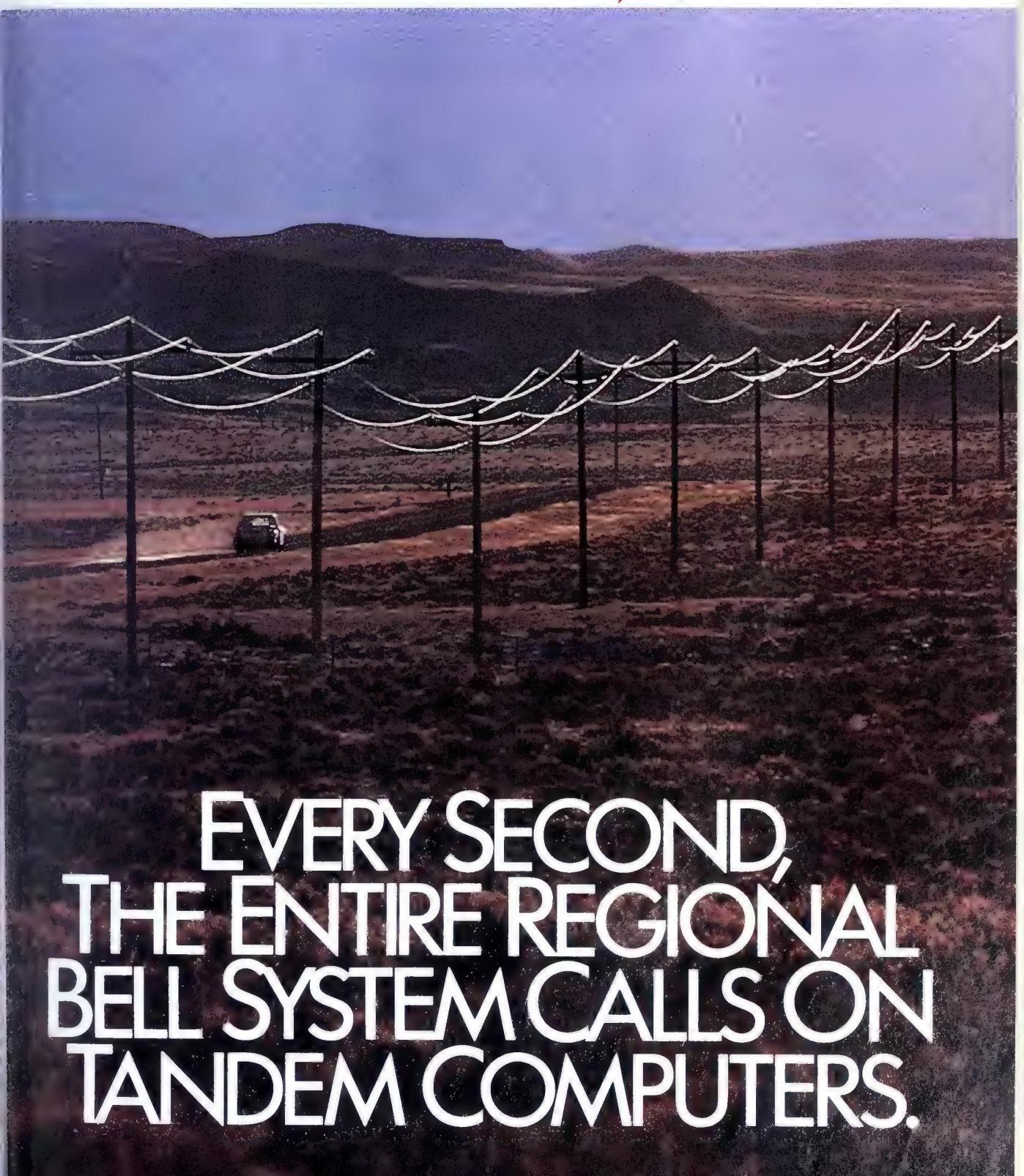
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TAMING SPACE AND TIME TO MAKE TOMORROW'S CHIPS

Intel Corp. and other chipmakers continue to make startling advances in semiconductor technology. And by the year 2000, silicon chips could pack 1,000 times more transistors than now. But you ain't seen nothing yet. Getting set to pick up

where today's circuits leave off are two radically different techniques. In the 1990s, vacuum tube may get updated to tubes-on-a-chip. And in the 21st century, chips could invade the weird realm of quantum mechanics.

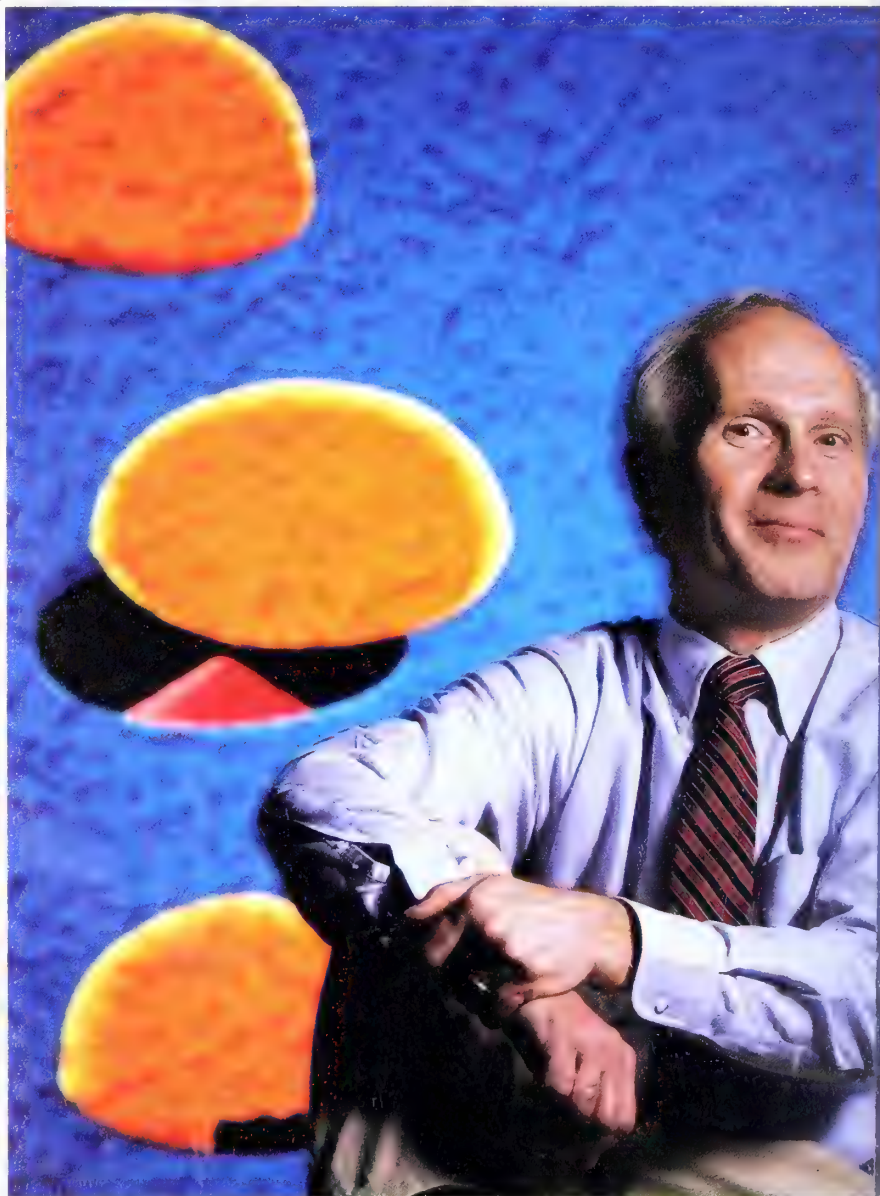
VACUUM MICROELECTRONICS

In the days when Glenn Miller and Jack Benny ruled the airwaves, the vacuum tube was king. Radios, TVs—even the first computers—were built with the glowing glass tubes. But the solid-state electronics revolution all but relegated the cumbersome devices to museums. Transistors and then integrated circuits etched onto silicon chips let engineers build powerful radios that fit in the palm of the hand and reduce room-size computers to laptop PCs.

Now, in a curious twist, a growing band of physicists and engineers are turning back to the vacuum tube. But these are very different from their clunky ancestors. Much like integrated circuits, today's tubes are carved into silicon wafers, and they are as tiny as the electronic devices on a computer chip—10 billion of them could fit onto five-inch wafer of silicon.

'QUIET REVOLUTION.' "It's a whole new microelectronics," says Henry F. Gray, a physicist at the Naval Research Laboratory in Washington and one of the pioneers in the field. Indeed, Gray and others foresee sweeping potential for the new technology. Because electrons travel much faster in a vacuum than through solids, engineers believe they can build the fastest computers yet. Moreover, vacuum electronics are not as vulnerable to temperature extremes and radiation that can destroy a computer chip. Among the possible applications:

THE NAVAL RESEARCH LAB'S GRAY: "IT'S A WHOLE NEW MICROELECTRONICS"



screens for high-definition television so thin they can hang on the wall, dizzyingly fast supercomputers, super telecommunications gear, and a new generation of more durable and exotic military electronics and scientific instruments.

The idea of making microscopic vacuum tubes is not new. Thirty years ago, Kenneth R. Shoulders began developing them at the Massachusetts Institute of Technology and continued his research at SRI International in Menlo Park, Calif. Like many others, Shoulders was trying to make smaller electronic circuits that would use less energy and generate less heat. But the invention of semiconductor chips achieved the desired result. The funding dried up, says Shoulders, who is now a consultant, and he abandoned the effort. "It was beyond the technology of the time," says Charles A. Spindt, a senior research engineer who carried on Shoulders' work at SRI.

Ironically, the intricate processing

technology used to build computer chips is what's now making vacuum microelectronics possible. NRL's Gray, for example, used now-standard photolithography and etching techniques to produce the first vacuum microelectronic transistor. Now, vacuum microelectronics has galvanized researchers in key laboratories in the U.S., Europe, Japan, and the Soviet Union. "It's a quiet revolution," says Robert B. Marcus, a physicist at Bell Communications Research Inc., the research arm of the deregulated telephone companies. "I think it's going to be big."

Shrinking the vacuum tubes to microscopic proportions results in devices that behave very differently from their huge ancestors or conventional circuits. In the large world, electrons flow through wires like water through a pipe. But in vacuum microelectronics devices—and in a new breed of computer chip that uses "wires" only a few atoms thick (page 70)—electrons obey the rules of quan-

tum mechanics, a branch of physics that describes how atomic and subatomic particles behave in very small dimensions. Electrons, for example, can "tunnel" through matter, disappearing from one side of a thin barrier and instantaneously appearing on the other.

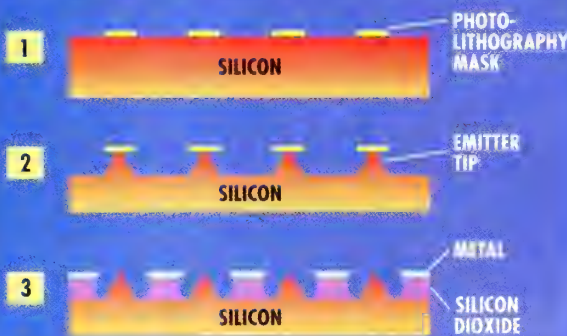
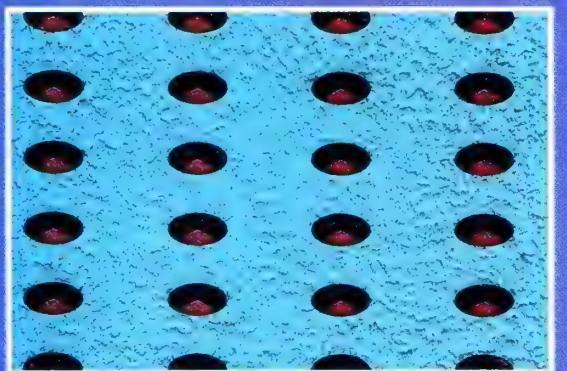
Unlike vacuum tubes of old or the cathode-ray tubes in today's TV sets, the tiny tubes-on-a-chip do not need heat to spew out a beam of electrons. Instead, they emit a beam of electrons when exposed to an electrical field—hence they are called field emitters. The tiny devices can be made of materials such as high-temperature superconducting ceramics as well as silicon or metals.

In addition, the devices don't require the strong vacuums that old-fashioned tubes did. At a microscopic level, molecules in the air are so far apart that electrons zip to their destination—a micron away—without much chance of collision along the way. "This new technology is so simple. Once it gets smaller and smaller, it gets better and better," says Takao Utsumi, vice-director of research for Canon Research Center in Atsugi, Japan. "There's almost no limit."

PIXEL POWER. Flat-screen television sets are likely to be the first application of the microelectronics devices. Researchers at SRI in the U.S., Philips and Thomson-CSF in Europe, and in Japan all have video display programs under way. They may have commercial products by the mid-1990s. While today's TV sets use a single electron beam scanning rapidly back and forth across the screen, the new displays would use millions of microscopic cathodes, each firing straight ahead, to cause phosphors on a flat glass plate to light up. Such displays could be windowpane-thin and operate at much lower power levels, producing a virtually unlimited number of pixels.

At SRI, Spindt uses standard silicon wafers to form the heart of a vacuum microelectronics video display. His team deposited an ultrathin—three-quarters of a micron—insulation of silicon dioxide onto the wafer, then coated it with an even thinner layer of metal. Next, they used a beam of electrons to drill holes 1 micron in diameter through the silicon dioxide. In each hole they built up a tiny cone of molybdenum metal that emits electrons when the metal film around the holes' edges carries an electrical field. "This technique has a very good chance of being the best way to go for high-definition television," says Spindt.

Other researchers have their eye on vacuum microelectronics for building superfast computers that would operate at lower voltages than those currently in use. Among his other ideas, Gray has already submitted a patent for computer memories based on the vacuum microelectronics. It will probably be eight



BACK TO THE FUTURE

To build the tiny vacuum tube cathodes pictured above, NRL researchers use standard chipmaking techniques. (1) A photolithographic process masks off dots on a silicon wafer. (2) Etching away the silicon creates pointed pyramids. (3) The area around those pyramids or emitter tips is built up with an insulating layer of silicon dioxide and topped with metal coating. In an electrical field the emitter tips spew a beam of electrons.

years or so before the technology reaches the point of fully integrated circuits, says Donald Young, senior staff scientist at Britain's Thorn EMI Central Research Laboratories. "But once we get there, we've got it made."

Vacuum microelectronics may also help researchers build computer devices that switch on and off in response to light instead of electrons. These could directly process data sent through optical fibers or by lasers. "No other known device has such broad response to such a wide range of signals," says Thomas E. Sullivan of Temple University, who envisions the technology becoming the basis for electro-optic computers. Scientists at Temple, Pennsylvania State University, and AT&T Bell Laboratories are experimenting with such applications.

NO MYSTERY. The military is interested in vacuum microelectronics because of the devices' "radiation resistance, ability to operate at high and variable temperatures, and potential for speed," says Rosemary A. Lee of General Electric Co.'s Hirst Research Centre near London. Military communications and control systems based on vacuum tubes would not be knocked out by the "electromagnetic pulse" of exploding nuclear weapons. In addition, vacuum microelectronics may be the basis for an array of other exotic military applications, including small, lightweight radars for aircraft and cruise missiles, electronic countermeasures equipment, and a variety of sophisticated sensors.

Because the devices are capable of switching on and off at such high speeds (150 femtoseconds, or 150 quadrillionths of a second), vacuum microelectronics telecommunications systems could transmit vast amounts of data. Gray, for example, has proposed using vacuum microelectronics as the basis for a supercellular telephone network that would operate at 60 gigahertz, a frequency at which the signals are strongly absorbed by the atmosphere. Operating at this frequency would eliminate the problem of signals causing interference when they spread out over a wide area. The technology could also be used for more secure satellite-to-satellite and satellite-to-earth communications.

Although much work remains to be done, researchers are optimistic that vacuum microelectronics will begin to have an impact relatively soon. After all, vacuum tube technology is no mystery. At the microscopic level, the challenge is now how to fabricate the devices. In the '90s electronics may indeed be heading to the future.

*By William D. Marbach in New York
and Richard Brandt in San Francisco.
Special Reports*

QUANTUM EFFECT CHIPS

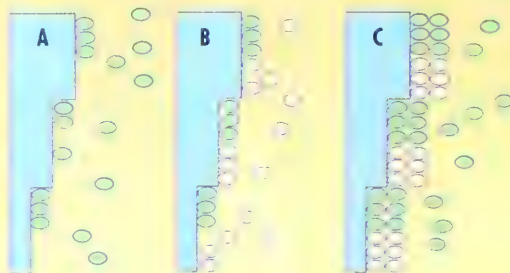
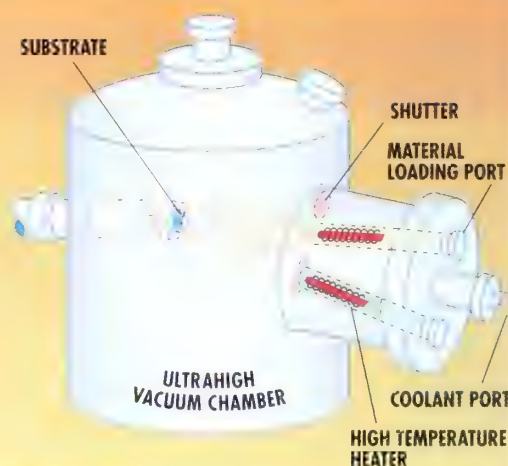
In today's best microprocessors, the transistors are tiny enough—about 1/100 the width of a human hair—that a million or so can be crammed onto a fingernail-size slice of silicon. But that's child's play compared with what researchers have in mind. They dream of a computer-on-a-chip that has transistors only a few atoms across. With such ethereal switches, one chip could be packed with billions of transistors, or more number-crunching power than today's biggest supercomputer.

research at AT&T Bell Laboratories "Well, we don't know yet."

But already there are some very tantalizing indications. Texas Instruments Inc. recently grabbed headlines by fabricating a working quantum-effect transistor, and "quantum wires" only a handful of atoms thick were produced a few weeks ago at the new Center for Quantized Electronic Structures at the University of California at Santa Barbara. Theoretically, TI's quantum-tunneling transistor can switch on and off a trillion times per second. That's 1,000 times quicker than today's commercial transistors. "When we finally burst the bubble of quantum electronics, it will be like moving from one universe to an entirely new one," asserts Hector Ruiz, director of semiconductor technology for Motorola

WHEN ATOMS ARE BUILDING BLOCKS

Elements such as gallium and arsenide are loaded into a molecular-beam epitaxy (MBE) system and vaporized. When a shutter opens for a precise interval, the vacuum sucks out a stream of hot, ionized atoms that "paints" the substrate. To make "quantum wires" the MBE machine (A) first



lays down a pattern of aluminum arsenide. The gaps between are filled with gallium arsenide (B), and successive layers of both molecules are deposited (C) to build the finished wire.

There's a hitch, though. Achieving this will require a quantum leap—to quantum mechanics. In this weird, unpredictable world of the ultratiny, electrons flit back and forth between being a dot of solid matter and an incorporeal field of energy. They "tunnel" through time and space, inexplicably vanishing from here and willy-nilly popping up there—instantaneously, without ever passing through the intervening space. Yet researchers are bent on harnessing this seeming chaos. "What do we do when the traditional physics governing the behavior of electrons no longer holds?" asks David V. Lang, director of solid-state electronics

at AT&T Bell Laboratories. "Applications will be limited only by our imaginations."

Still, even George H. Heilmeier, TI's chief technical officer, cautions that researchers have barely scratched the surface of quantum electronics. "We're not about where we were with silicon technology in the 1940s," when Bell Labs was working on the first solid-state transistor, he says. So don't look for "gigachips" stuffed with billions of transistors to arrive much before the year 2000. Certain critical issues, adds James Meindl, provost of Rensselaer Polytechnic Institute and former director of Stanford University's Center for Integrat-



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Systems, "haven't even been solved conceptually, let alone practically." Indeed, few, if any, of the fundamental principles underlying today's integrated circuits will apply in the quantum realm.

To fill in the gaps, scientists at high-power research labs around the world—including Germany's Max Planck Institute, Japan's Electrotechnical Lab, and the Netherlands' Philips, plus IBM, MIT, and Sandia Laboratories in the U.S.—have been methodically plugging away for a decade. They use some of the most exquisitely precise equipment ever devised, such as molecular-beam epitaxy (MBE) machines and metal organic chemical-vapor deposition (MOCVD) systems. This equipment can already lay down semiconductor materials in layers that are the thickness of a single atom. NEC Corp. and others are now working on a new approach, called digital epitaxy, that will provide still tighter control.

COLLISIONS. Regular chipmaking equipment can't come close to fabricating quantum transistors. The latest systems can be pushed to produce structures a

Once science cracks quantum electronics, 'it will be like moving from one universe to an entirely new one'

mere 0.5 micron—or half of a millionth of a meter—wide. But the quantum realm begins below 0.01 micron. Distances then get so infinitesimal that physicists measure them in angstrom units, or 0.1 billionths of a meter. If a grain of salt were as tall as Chicago's Sears Tower, 1 angstrom would be about as thick as a sheet of paper.

To achieve the phenomenal speeds promised by quantum electronics, transistors must shrink 100-fold or more. Otherwise, there is a high probability that electrons zipping across the transistor will bump into atoms in the semiconductor crystal. In current chips, these collisions happen so frequently—every 100 angstroms in silicon, on average, and every 1,000 angstroms in gallium arsenide—that the electron flow is seriously impeded. Result: Switching time slows to a fraction of what's possible.

But in 1981, Lester F. Eastman, an electrical engineering professor at Cornell University, advanced the notion of "ballistic" transistors, or transistors so minuscule that electrons could shoot across them without collisions. Until recently, nobody could make a transistor that tiny, so the only way to test East-

man's idea was to create a switchlike junction between ultrathin layers of different semiconductor materials. Such so-called heterojunction was created by Mordehai Heiblum, a scientist at IBM Thomas J. Watson Research Center. In 1986, Heiblum and Eastman demonstrated ballistic transport through the inner layer in a sandwich of gallium arsenide and aluminum gallium arsenide.

SENSE OF PLACE. Last year, Nippon Telegraph & Telephone Co. crafted an actual transistor in a heterojunction material and obtained marginally ballistic properties, with a switching rate of 105 billion times a second. Bell Labs topped that by using the needle-sharp beam of energy from an electron-beam machine to carve a tinier, 500-angstrom transistor on a similar heterojunction—and recorded partially ballistic results. Its switching speed was measured at 140 billion times a second. With its E-beam machine, Bell Labs has also made a smaller switch—just 300 angstroms across—that cycles ballistically through a trillion on/off operations a second. It is useful for research, notes Lang, but he admits that its design is impractical. It is simply too sensitive. It can be triggered by the arrival of a single electron.

That points up how disconcerting quantum mechanics can be. Since electrons hop around randomly, quantum transistors must be engineered to resist activation when one or two electrons drop in unexpectedly, or if a couple abruptly vanish into the ether, says Robert T. Bate, a TI research manager. The quantum-effect device may be the smallest transistor yet—only 200 angstrom wide—but it requires at least a dozen electrons to set it off.

But researchers haven't given up on the idea of hypersmall devices that would cage solitary electrons in a "quantum dot" as small as 10 angstrom. There are indications, says TI's Bate, that an array of quantum dots grouped closely together could communicate among themselves without wirelike connections. That would help alleviate a major headache for tomorrow's chip designers: figuring out how to hook up billions of switches. In today's chips, connecting a million transistors requires several meters of wiring, which has to be laid out painstakingly to avoid eating up a lot of silicon "real estate." Stringing together 1,000 to 10,000 times as many transistors and stuffing that layout on a little chip would be mind-boggling.

As for the random tunneling problem, researchers may be able to concoct some way to exploit another curious aspect of quantum theory: Once an electron has been in a given place, it somehow retains a mysterious link to that place. Nobody

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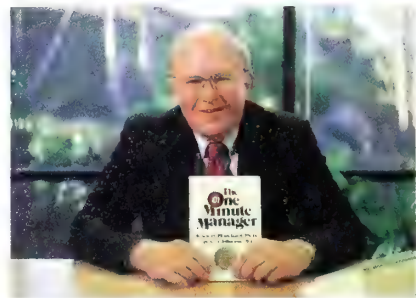


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can explain this, and it clearly conflicts with elements of Einstein's theory of relativity. However, in tests designed to pit quantum mechanics against relativity, quantum mechanics has won. It may be possible for quantum computers to use an electron's sense of place to tell if it's where it's supposed to be.

POWER TO BURN. If quantum electronics seems like Alice-in-Wonderland technology, the basic principles are already being applied in superefficient semiconductor lasers. For laser diodes, "quantum effect devices are here today," declares Nick Holonyak Jr., a pioneer in the field who teaches at the University of Illinois. These devices bounce electrons back and forth inside a so-called quantum well, amplifying their energy until the proper lasing frequency is reached.

Despite the long-term potential of quantum electronics, many experts warn that current silicon technology isn't yet

Quantum chips will have so much power, says one expert that 'we can squander it' on user-friendly devices

down for the count. It will probably remain the semiconductor industry's workhorse into the next century. Today's 1-micron transistors are now shrinking to 0.7 micron, which will increase the number of transistors per chip to 10 million or more. After dropping to 0.5 micron by the mid-1990s, silicon chips may host 10 million transistors. Near the turn of the century, with 0.2-micron structures, even silicon may hit the gigachip level.

Nevertheless, silicon's limits are plainly visible, and the electronics industry will have to find an alternative to sustain further improvements in computing power. Lang of Bell Labs is confident that quantum chips "will be the dawn of a new technology." Packing a supercomputer's punch onto individual chips will usher in so much power "that we can squander it" on a new generation of user-friendly machines. They may even understand verbal commands and sense from your tone of voice or your facial expression how urgent a job is.

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By Otis Port in New York, with bureau reports



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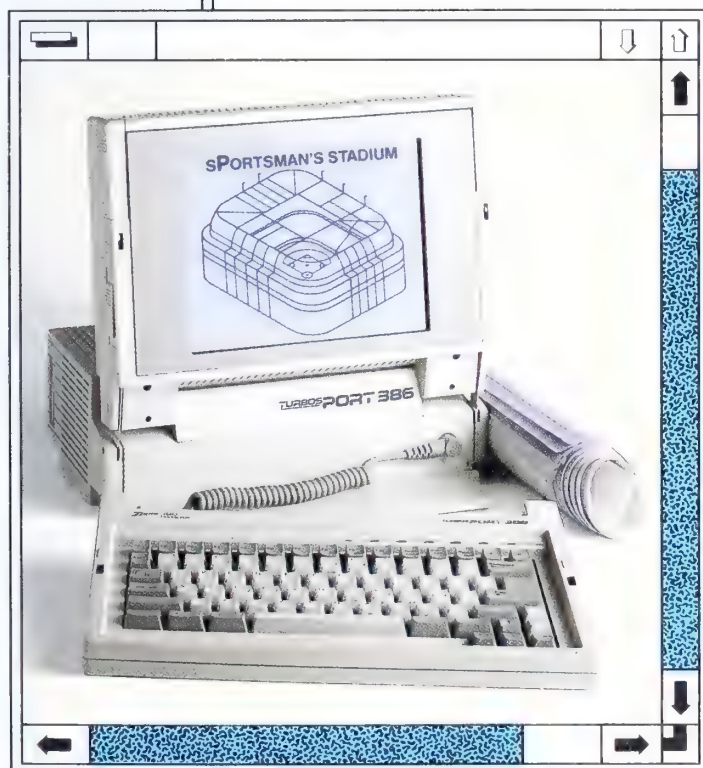
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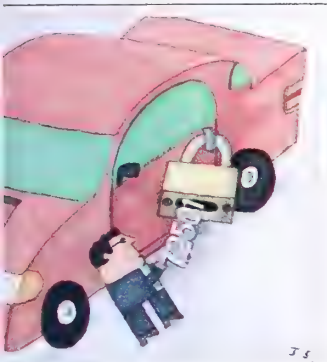
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TV TECHNOLOGY MAY KEEP CARS SAFER FROM THIEVES



Looking for a better car security system? Take another look at your TV. Using the same technology that sharpens TV images, GTE Corp. scientists have come up with a new theft-proof locking system. The device uses the properties of SAW—surface acoustic waves—to activate a tiny coil embedded in a car key. As the key turns to open the door or start the engine,

the coil sends out a coded digital signal needed to unlock or start the car. GTE makes similar SAW filters to lock in color TV channels on each channel.

GTE's auto-lock system, called SAFE for surface acoustic filter encoding, has the advantage of being completely passive: there are no codes to memorize or alarms to disarm. And unlike other antitheft locks, SAFE needs no electrical contact—even teeth on the key. Eventually, keys for individual drivers could be encoded to automatically adjust the seats and mirrors. So far, GTE has gotten "a strong response" in Detroit, says Scott L. Atkinson, marketing specialist with GTE's Electronic Components & Materials Div., who thinks auto makers may offer SAFE within two years. Also eyeing the system, says Atkinson, are foreign carmakers and major U.S. car insurers, who are battling \$6 billion a year in U.S. car-theft losses.

GETTING DIALYSIS PATIENTS BACK ON THEIR FEET FASTER

For the thousands of patients with kidney disease, dialysis machines are literally lifesavers, filtering out harmful substances in the blood. But the process is time-consuming and can have painful side effects. Now scientists at West German chemical giant Bayer have developed a new membrane material that is more efficient than today's cellulose membranes. It reduces side effects and could speed the process, too.

The trouble with cellulose membranes is that they are not good at filtering medium-size molecules from the blood. As a result, dialysis is slow—typically taking six to eight hours—and must be repeated frequently, which prevents many patients from working full time. But researchers at Bayer created a new synthetic membrane made of a plastic copolymer that they say is 25% more efficient. The material was developed especially for the Swedish company Gambro, the largest worldwide supplier of dialysis machines. Gambro's German subsidiary plans to offer the new membranes this spring.

HIS COMPUTER SYSTEM COULD SOLVE THE UNSOLVABLE

The Military Airlift Command has a humdinger of a traveling salesman problem on its hands: MAC flies roughly 1,000 planes in and out of 329 airports around the world. So what's the most efficient schedule for keeping those planes in the air as much as possible without skimping on service to any of those airports? Answering a question with even a small frac-

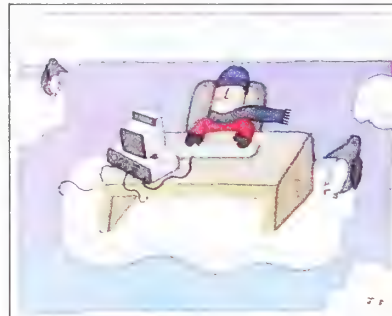
tion of those variables would bring a mainframe computer to its knees—there are too many possible solutions to evaluate.

Now the Air Force may have found a solution in a new computer system, called Korbx, built by AT&T Bell Laboratories. It is based on the work of Narendra Karmarkar, a Bell Labs mathematician who, in 1984, devised a way of "getting inside" such problems to spot shortcut solutions. The first commercial Korbx system has just been installed at MAC headquarters on Scott Air Force Base in Illinois. Fed a problem with 321,000 variables plus 14,000 time constraints, the computer chewed away for only an hour before spitting out a solution. "We're now in hog heaven," says Colonel Robert C. Roehrkasse, director of MAC's Analysis Group.

HAS JAPAN FOUND THE 'BRAINS' FOR THE COMPUTERS OF THE FUTURE?

Two of Japan's electronic kingpins say they have cracked the door to superconducting computers that will one day leave all other machines in the dust. Last month, Hitachi Ltd. and Fujitsu Ltd. successfully tested novel superconducting microprocessor units (MPUs), the "brains" in most computers.

The MPUs are bulky by today's standards, and both require expensive cryogenic cooling—they are made with low-temperature superconducting materials, not the new high-temperature varieties. But Hitachi's MPU, with 30,000 transistor-like switches known as Josephson junctions (JJs), can rip through 250 million instructions per second. That's five times the raw speed of today's fastest MPUs, such as the RISC (reduced instruction-set computing) chips from MIPS Computer Systems Inc. and Sun Microsystems Inc. Since each Hitachi instruction now contains only four bits of data, it would take eight of them to equal one of the 32-bit instructions handled by the U.S. chips. Fujitsu's superconducting MPU, also a 4-bit design, has fewer JJs—24,000—but its internal clock ticks just as fast: more than a billion times a second.



TAKING THE HEADACHE OUT OF INTEGRATING MACHINERY

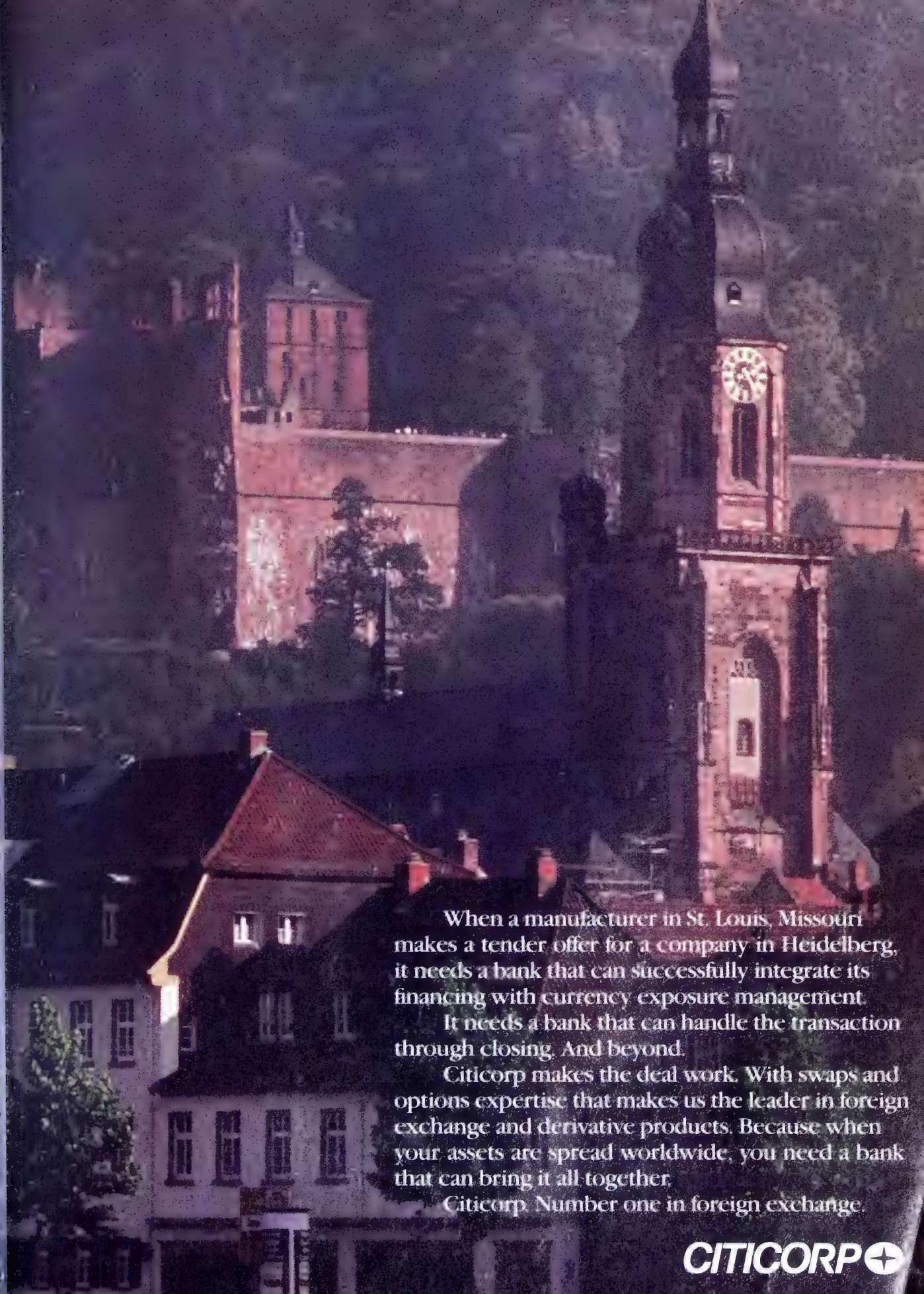
Computers have become essential to high-speed manufacturing. But manufacturers who use them must assemble a bewildering array of components: motors, controllers, power supplies. Compatibility can be a big headache, and so can wiring the parts together.

Enter the smart motor. Engineers at Intellico Inc., in Libertyville, Ill., have devised a motor for factory floor machinery that integrates the motor, power supply, and computer controller all in a single package. Armed with a Motorola 68000 microprocessor and onboard memory, the Intellimotor can be programmed from personal computers or other types of terminals. And it can be reprogrammed while the machinery is running, eliminating the expense of shutting down a fast-moving assembly line, explains Gregory Arends, chief technical officer of Intellico. Arends envisions a wide variety of applications for the integrated system, including robots, machine tools, automated assembly machinery, process control equipment, and automated parts inspection systems.



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PUZZLE IN MOVIELAND: THE CASE OF THE MYSTERY MOGULS

Hollywood is starting to wonder where Cannon's new Italian owners got all that money

Giancarlo Parretti began his career in the 1960s as the manager of a small hotel north of Rome. But after he was convicted of falsifying its balance sheets, he took a job as a waiter on a transatlantic liner.

These days, Parretti could probably buy a couple of ocean liners, with a few hotels thrown in. The assets he claims to control in real estate and travel are worth billions. Since 1987, he and his partner, Florio Fiorini, have added such independent film companies as Cannon Group Inc., France's Pathé Cinema, and—in a deal announced on Feb. 24—New World Entertainment Ltd. He plans to gobble up still more of Hollywood. "I want to create the biggest film group in the world," Parretti says. He even talks about buying MGM/UA Communications Co., a major studio.

Such bold plans raise questions with officials in a variety of countries: Who are Parretti and Fiorini? How did the two 49-year-old financiers amass so much cash? And what's their Hollywood strategy?

Some of the answers are disturbing. Parretti and Fiorini have been involved in major financial scandals in Italy and elsewhere. Former partners of both men have told BUSINESS WEEK that the financiers' network of private foreign holding companies hide so-

phisticated money-laundering operations. Parretti and Fiorini deny the charge.

Associates and government officials say that the two men built their fortunes from business deals arranged by high-ranking politicians, especially in Italy's center-left Socialist Party. Citing the pair's powerful connections, most sources for this story asked to remain unnamed. However, a French magazine recently quoted from a Spanish govern-

ment report to President Felipe González that said: "All the associates of Parretti, whether in Rome, Switzerland or Luxembourg, have been mixed up in big scandals over the last decade." Italian officials express concern about Parretti. "We are watching him closely and with keen interest," says an aide to Italian Prime Minister Ciriaco De Mita. "He's got a shadowy past." Parretti's attorney in Rome, Antonio Rappazzo,

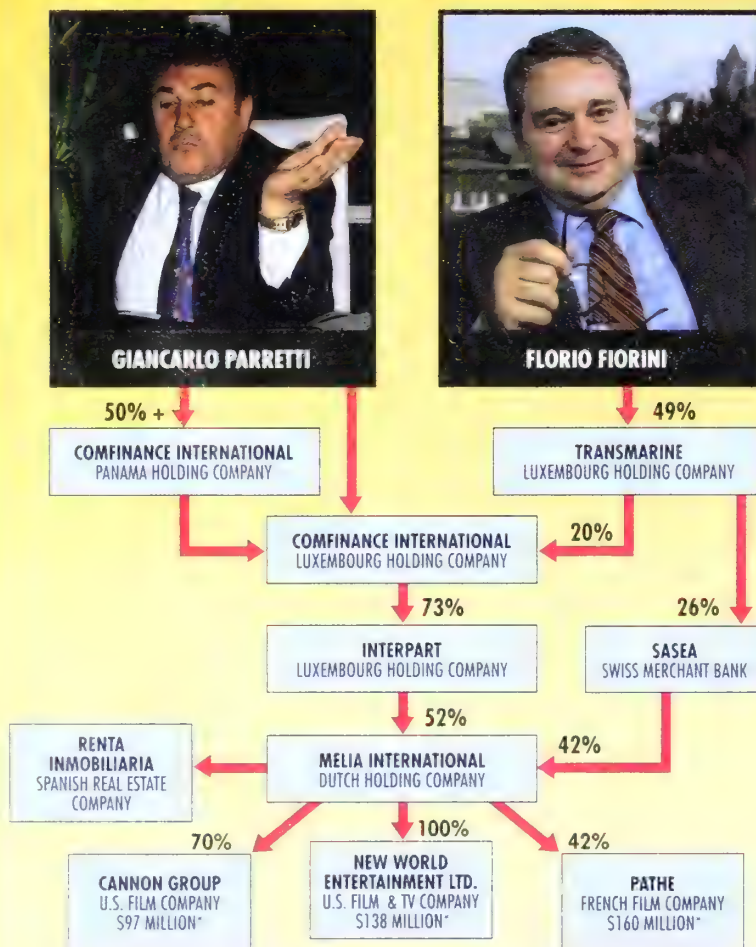
says the Italian government is harassing an innocent man.

Parretti was briefly jailed twice in Sicily in 1981 after he was charged with defrauding a bank that failed in Palermo and with misstating the balance sheet of his soccer team, Siracusa Calcio. He was acquitted on appeal in the Palermo case and is waiting for the other to be tried. In 1986 the police grabbed Parretti as he got off a plane at the Rome airport, charged him with extortion, and hustled him off to a Naples jail. This charge was later dropped.

NEW FACES. The smudges on Fiorini's record go back to the infamous Banco Ambrosiano scandal in 1982. Fiorini was chief financial officer of Italy's state-owned oil company ENI. He became involved in the affair by placing \$130 million of ENI's money into shell companies controlled by the troubled Milan bank, according to an Italian government con-

PARRETTI AND FIORINI: ON THE ROAD TO HOLLYWOOD

The two Italian financiers run a complex empire of interlocking companies. They claim to control assets in real estate and travel that are worth billions. In entertainment, the value of their holdings in Cannon, New World, and Pathé is nearly \$400 million.



*Estimated value of total Parretti-Fiorini investment, assuming New World acquisition becomes final.

mission of inquiry. The bank was run by Fiorini's close friend, Roberto Calvi. Despite ENI's deposits, Banco Ambrosiano failed, the largest banking collapse in Europe since World War II. ENI fired Fiorini after his role in the attempted rescue came to light. Italian authorities also publicly charged in 1982 that Fiorini and Calvi had transferred \$7 million to a Swiss bank account controlled by the Italian Socialist Party. Fiorini moved to Switzerland, where he and several partners bought SASEA, a publicly traded merchant bank. Calvi was later found hanging from a bridge in London.

Legal problems in Europe, however, have not followed Parretti and Fiorini to Hollywood. They had no trouble buying Cannon from Menahem Golan and Yoram Globus in 1987. The U.S. Securities & Exchange Commission says it isn't empowered to investigate Parretti's and Fiorini's finances: The bulk of their funds come from companies registered in Luxembourg and Panama.

Now that Parretti and Fiorini are in the movie business, their money trail will be harder to follow. Film companies take in lots of cash from ticket buyers around the world and can spread it over so many projects that it's hard to know where it goes. Parretti will make it even tougher for outsiders to scrutinize his operations. For tax purposes, he plans to gather his movie assets in a Dutch holding company that he created in late February.

That company will hold some glittering assets.

The Pathé-Cannon combination already gives the Italians more than 1,500 theaters throughout Europe, plus a library of about 1,450 films including such titles as *Death Wish* and *American Ninja*. The deal for New World adds TV shows such as *The Wonder Years* and *Santa Barbara*, and popular schlock movies including *Hellbound: Hellraiser II*. Parretti intends to fold New World into his new U.S. production company, Pathé Entertainment Inc., which he formed in late January.

STILL SPLURGING. Alan Ladd Jr., who approved production of hits such as *Star Wars* and *Moonstruck*, will run Pathé Entertainment, and seems to have worked out a sweet deal. He will be entitled to 20% of all profits. Parretti plans to pump \$400 million over four

years into the fledgling operation and make about 15 films. The financier also announced on Feb. 27 that he will invest at least \$160 million for 17 films to be produced by Golan.

Parretti is still on a buying spree. He has already bid \$22 million to take De Laurentiis Entertainment Group out of Chapter 11. And MGM/UA, which he's now eyeing, could cost as much as \$1 billion in cash and debt. Parretti is also trying to raise \$300 million in Europe to pay for movie acquisitions in Italy, Spain, West Germany, and Britain. Robert Maxwell, the newspaper and book

that went as high as \$8 a share. The stock currently trades at around 5.

The two Italians had no experience in the movie business when they bought the troubled Cannon, and they have performed no magic. The studio was losing \$98.3 million in 1987, and estimates put Cannon's 1988 losses at \$100 million.

That figure will drop when Cannon includes profits from the sale of some U.S. and British movie theaters to one of Parretti's holding companies.

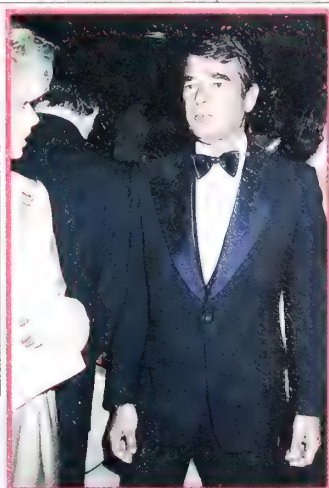
TWIN ROLLS-ROYCES. Undismayed, Parretti says that the growing demand for films abroad offers new opportunities for a Europe-based entertainment group. With his network of movie theaters, for example, Parretti can show a film in different countries at the same time. That would make it cheaper to promote the movie, using satellite broadcasts and international newspapers. Parretti's associates argue that this scenario would give him real clout with important filmmakers.

Parretti, however, seems to be rehearsing for a more glamorous role than that of a mere overseas distributor. "When I go to Hollywood, I don't want to be treated like a hired hand, but as a chairman," he says.

He is learning the part from a master: Dino De Laurentiis. The 69-year-old director first told Parretti about Cannon's troubles and suggested the eventual bailout. Since then, De Laurentiis has introduced Parretti to many of his Hollywood pals, including Ladd and superagent Michael Ovitz. A few weeks ago, Parretti accompanied De Laurentiis to a Beverly Hills Rolls-Royce dealership where he bought a \$200,000 brown Rolls just like the one De Laurentiis drives.

Parretti is showing his appreciation by trying to salvage the De Laurentiis Entertainment Group. He has advanced De Laurentiis \$20 million to make a movie for Pathé, and he intends to set up his new Pathé operations in an office building in Los Angeles that he just bought from the filmmaker.

De Laurentiis is the latest name on a long list of influential mentors who have



AS PRODUCTION CHIEF OF PATHE ENTERTAINMENT, ALAN LADD JR. WILL TAKE 20% OF ITS PROFITS



ITALIAN DEPUTY PRIME MINISTER GIANNI DE MICHELIS WAS ONE OF THE WELL-PLACED FRIENDS WHO OPENED DOORS FOR PARRETTI



FINANCIER MAX THERET, ENMESHED IN A FRENCH STOCK SCANDAL, RUNS PATHE FOR PARRETTI

publisher, and Italy's tycoon of private TV, Silvio Berlusconi, have indicated that they would like a piece of the action.

Parretti and Fiorini are showing a lot of faith in the future of the film business. In each of their acquisitions, they paid handsomely for companies with problems. When New World went on the block in late January, its \$125 million debt had pushed its shares down to under 3. Parretti has offered \$138 million, or \$8.20 a share in cash and noninterest-bearing notes. In the case of Pathé, analysts in Paris say the \$160 million price that Parretti, Fiorini, and their partners paid was twice what the company was worth. And the financiers pumped an estimated \$97 million into Cannon for loans and stock purchases. They ended up with 42% of the company at prices

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guided Parretti. His studies began in Sicily, after he met Graziano Verzotto, a passenger on the ocean liner where Parretti was a waiter. Verzotto was trying to establish a hotel business in Syracuse. As the city's political boss, he was discreetly building his own substantial business holdings and needed a front man. He put Parretti in charge of the posh Villa Politi Hotel, whose guest list once included Winston Churchill.

Verzotto lost his political clout in 1975. He moved to Beirut and then Paris. But Verzotto made sure his properties ended up in friendly hands, putting Parretti in charge of the Villa Politi and two other resort properties. In 1980, Verzotto's wife named Parretti president of the Syracuse soccer team that Verzotto owned. "He was Verzotto's heir apparent," says Sicilian journalist Sergio Buonadonna.



YORAM GLOBUS, LEFT, AND MENAHEM GOLAN SOLD CANNON WHEN IT BEGAN LOSING MONEY

Sicily and resurfaced in Hong Kong. De Michelis, sources say, had found him temporary work there as the head of a tuna-fishing company.

Parretti apparently decided there were more exciting opportunities in Paris, where the French Socialists had come to power under François Mitterrand in late 1981. Armed with introductions from Craxi and De Michelis, Parretti had business cards printed up identifying him as "Secretary General of the Italian Socialist Party in France." He won points with France's Socialist leaders in early 1987 when he joined financier Max Théret in a \$7 million effort to prop up *Le Matin*, a Socialist-supported national paper. Although the paper ultimately folded, Parretti became good friends with Théret



DINO DE LAURENTIIS, PARRETTI'S LATEST MENTOR, SUGGESTED THE CANNON BAILOUT

That was not an enviable legacy: A government leader alleged to Italy's Parliamentary Commission on the Mafia that Verzotto had links to at least one powerful crime family. These days, Parretti minimizes his relationship with Verzotto: "I never had any business with him."

GONE FISHING. With the help of well-connected friends, meanwhile, Parretti started building bridges to the upper levels of the Italian Socialist Party. A member of the party since 1958, he demonstrated his loyalty in 1976 by launching *Il Diario*, a sympathetic newspaper in Palermo with regional editions. He soon mingled with party heavyweights such as Bettino Craxi, the former Prime Minister, and Gianni De Michelis, the current Deputy Prime Minister. Parretti made De Michelis' brother, Cesare, president of *Il Diario*'s Venice edition. When the paper went bankrupt in 1982—allegedly owing \$2.3 million—Parretti left

and *Le Matin*'s chairman, Paul Quilès, who is Mitterrand's postal and communications minister.

Those contacts paid off last year when Parretti and Fiorini went after Pathé. Some French officials didn't want one of the country's most venerable companies to fall into Italian hands. So Parretti quickly brought in Théret and his associates to serve as a French front for the deal. Théret and his partners now own 70% of Pathé. The French financier's name may be more widely known these days in connection with the massive Pechiney-Triangle Industries Inc. insider-trading scandal. He was one of the top buyers of Triangle shares in late 1988 at \$10 a share—days before Pechiney announced its plans to buy the U.S. can company for \$56 a share.

Parretti is relatively new to the high-stakes takeover game. His first big move came in 1986, when he took control of some ailing insurance companies and

small banks owned by Italy's Cabassi Group. The company had decided to sell after the government threatened to impose strict regulations. Along with cash, Parretti offered Cabassi assurances that he could protect the company from government intervention.

Parretti claims that deal paved the way into the motion picture business. He says he made \$200 million after he sold some of the Cabassi banks and insurance companies to Olivetti Chairman Carlo De Benedetti. But a former Parretti aide who worked on the deal says Parretti at the most made \$20 million. De Benedetti declined to comment.

The Cabassi deal brought Parretti together with Fiorini, a soft-spoken Tuscan who helped arrange some of the sales to De Benedetti. Parretti and Fiorini soon went on a spending binge in Spain. In 1987 they made two major purchases, paying \$65 million for the world's third-largest travel group, Meliá International, and later \$103 million for one of Spain's richest real estate companies, Renta Inmobiliaria.

Although the partnership has been profitable, Fiorini is apparently having second thoughts. The recent uproar in the French press over Théret and warnings from colleagues who say that Parretti has close ties with Sicilian crime families have disturbed the financier, say his aides. Fiorini told *BUSINESS WEEK* that he's not concerned, but took care to put some distance between himself and Parretti: "Parretti is not a partner," Fiorini insists. "We're just his financial associates." Fiorini also minimizes the link by suggesting that only 5% of SASEA's investments are in film. "Fiorini thinks he can control Parretti and that he can get out whenever he wants," says one big investor in SASEA. "But he's been saying that for two years now."

Fiorini would find it difficult to breathe free: He's involved in every one of Parretti's biggest deals. Fiorini's wife, Elena Badaloni, is listed as chairman of the Luxembourg-based syndicates organized to buy Cannon stock. Parretti also claims to have a stake in SASEA, while Fiorini denies.

Even with Hollywood's spotlight on them, Parretti and Fiorini remain mysterious figures. Parretti believes he hasn't gotten the respect he deserves. "People thought I was a stupid little idiot arriving in America," he says. "No one ever thanked me for saving Cannon." Parretti certainly isn't stupid. It won't take him long to discover that thanks are rare in Hollywood.

By John Rossant in Rome, with Frank Comes in Paris, Ronald Grover in Los Angeles, David Lieberman in New York, and Karen Wolman in Rome



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WHEN ALAN TREMAIN CHECKS IN, THE GLITCHES CHECK OUT



Crummy room service, ugly wallpaper, misplaced reservations—these are the sorts of things that make Alan Tremain's day. Tremain, 53, is the owner of Hotels of Distinction, a company that specializes in turning around struggling hotels. As he puts it: "We are looking for trouble."

Over the past 16 years, Tremain has spruced up and managed inns from Boston to Barbados. But now he wants to buy distressed hotels of his own. Armed with \$40 million from a consortium of European investors, Tremain is on the

rowl for acquisitions he can turn around within five years and sell for a profit.

Tremain, a native of Cornwall, England, engineered his first turnaround at Boston's Copley Plaza. When John Hancock Mutual Life Insurance Co. bought the Copley in 1972, the grande dame of Boston hotels had become a dilapidated money-loser. Hancock hired Tremain, who added a top-notch restaurant, tightened financial controls, and embarked on a massive renovation. Under his management, revenues climbed from \$4.5 million to more than \$20 million last year.

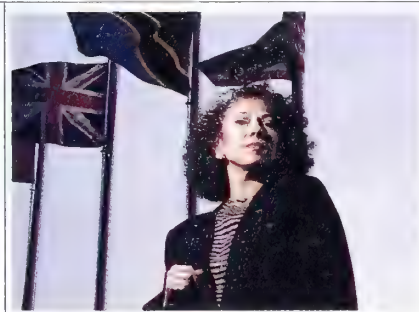
When the hotel was put up for sale last year, Tremain tried to buy it. But he lost out to a bid of \$56 million, so he recently moved his operations out of the hotel and relocated in Palm Beach, Fla. "I am not going to pay more than [the Copley] is worth just for the sake of owning it," says Tremain. After all, it doesn't need a turnaround specialist anymore.

By Robert Duffy in Boston

CHARLYNN GOINS COULD WRITE THE BOOK ON JOB MOBILITY

These are not the calmest of times for employees of Integrated Resources Inc., the New York financial-services firm. Insurer ICH Corp. is trying to acquire a controlling stake in Integrated, and no one knows what will happen to its various departments. But Charlynn Goins, head of international marketing, isn't worried. "I have no reason to believe the international business will be affected," says Goins, 46.

Even if Goins were to lose her job, she shouldn't be too concerned: She has an unusual knack for landing on her feet. Fifteen years ago, after raising two children, Goins grew tired of the housewife routine and decided to become a lawyer. With financial and moral support from her husband, a doctor, she



graduated from Columbia Law School and went to work as a tax attorney at Manhattan's Proskauer, Rose, Goetz & Mendelsohn. Although Goins enjoyed legal work, "I felt sort of like a consultant," she says. "I started thinking I'd like the business world, where I could make decisions myself." In 1982 she left to become assistant to Arthur H. Goldberg, president of Integrated, which was a client of her law firm.

Goins speaks French fluently and has traveled extensively overseas. So when Integrated began planning a move into foreign markets in 1985, she was a natural to head the effort. She has helped the firm open offices in Tokyo and Hong Kong, and she has set up joint ventures with several companies that sell Integrated products overseas. One of her most recent projects is an annuity that is specially tailored for foreign investors who want to defer income in U.S. dollars. Foreign investors' favorite products are partnerships that buy American real estate, she says. Overseas customers now account for some 5% of the funds in Integrated's latest real estate partnership, or about \$7 million, and Goins thinks they could eventually reach 20%. That is, if she's not off on a new career by then.

IF YOU MISSED WHAT THEY SAID, CONTACT JIM SMITH

Did George Bush really call Ted Koppel "Dan" on *Nightline*? What precisely were Oprah Winfrey's diet secrets? Jim Smith, 41, has the answers—within hours of the show's conclusion. He is the president and founder of Journal Graphics Inc., a New York company that sells transcripts of some 35 different TV news and talk shows.

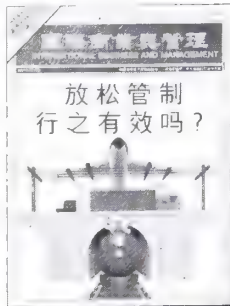


Working out of their homes, Smith's nine transcribers tape TV programs, type the dialogue into computers, and send the copy via modem to Journal Graphics' headquarters. There, each show's transcript is published on Smith's laser printer and is ready for sale within hours. Smith doesn't even have to advertise: His "client" programs all broadcast Journal Graphics' phone number and address. The average price per transcript is \$3. On the more popular shows, the producers take a royalty. But in many cases, the shows are so happy that the transcripts are available that they let Smith pocket the entire fee. He predicts that Journal Graphics will gross more than \$2 million this year.

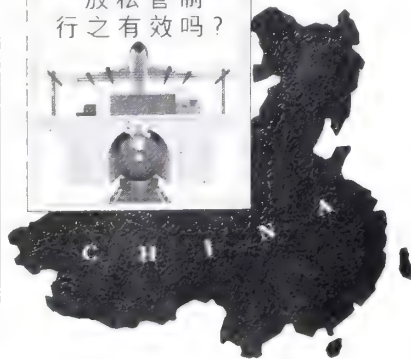
Not all of Smith's ventures have turned out so well. After growing up in Brooklyn, he started three small newspapers in New York City. They all failed. He also ran for mayor of New York in 1981, and later for city council as the "Subway Candidate." No luck there either. But after closing newspaper No. 3, which was tailored to New York cops, he kept its typesetting machine and opened Journal Graphics. Watching TV one night in 1979, he got the idea to print transcripts with his typesetter.

MacNeil/Lehrer Newshour was his first client. Ten years later, Smith has a virtual lock on the transcribing business. This January he won the rights to what should become his biggest money-maker yet: *Donahue*. Now he hopes to work out a deal with the three networks' evening news shows. But he does draw the line somewhere. Says Smith: "I would have a hard time saying yes to *Morton Downey Jr.*"

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Economics

LABOR

PLENTY OF WORKERS ARE WAITING IN THE WINGS

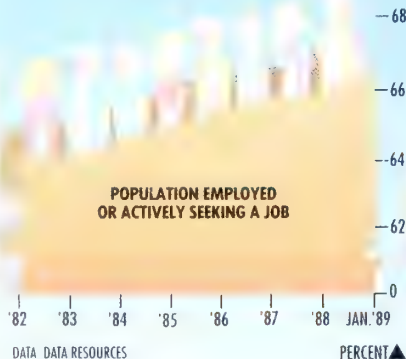
A huge untapped pool should help prevent wage increases

The economic expansion is being treated like a dinner guest who has overstayed his welcome. Six years ago, when 10 million Americans were out of work, any increase in the number of jobs would have been greeted with glee. But when employment soared in January, the response was a groan of dismay. And when producer and consumer prices jumped in January, many economists had their worst fears confirmed: The economy was growing too

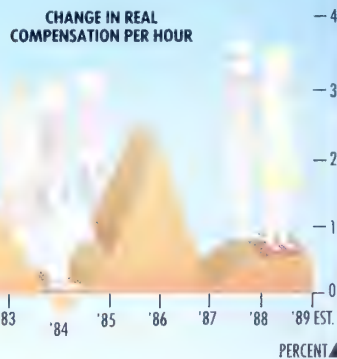
Kellner, chief economist at Manufacturers Hanover Trust Co.: "There are plenty of people out there to fill all the jobs that industry can supply."

Since the expansion began in November, 1982, wage increases have been surprisingly moderate. That was to be expected in the early years of the expansion. The recovery was beginning from a very low base, and labor was readily available. In certain regions such as the Midwest, manufacturing er

MORE PEOPLE ARE ENTERING THE LABOR FORCE...



...AND THAT IS KEEPING A LID ON WAGE GROWTH



fast for its own good, labor shortages would soon lead to wage pressures, and that would set off an inflationary spiral. Even the Federal Reserve Board's recent half-point increase in the discount rate, to 7%, is not large enough, some worry, to halt the process.

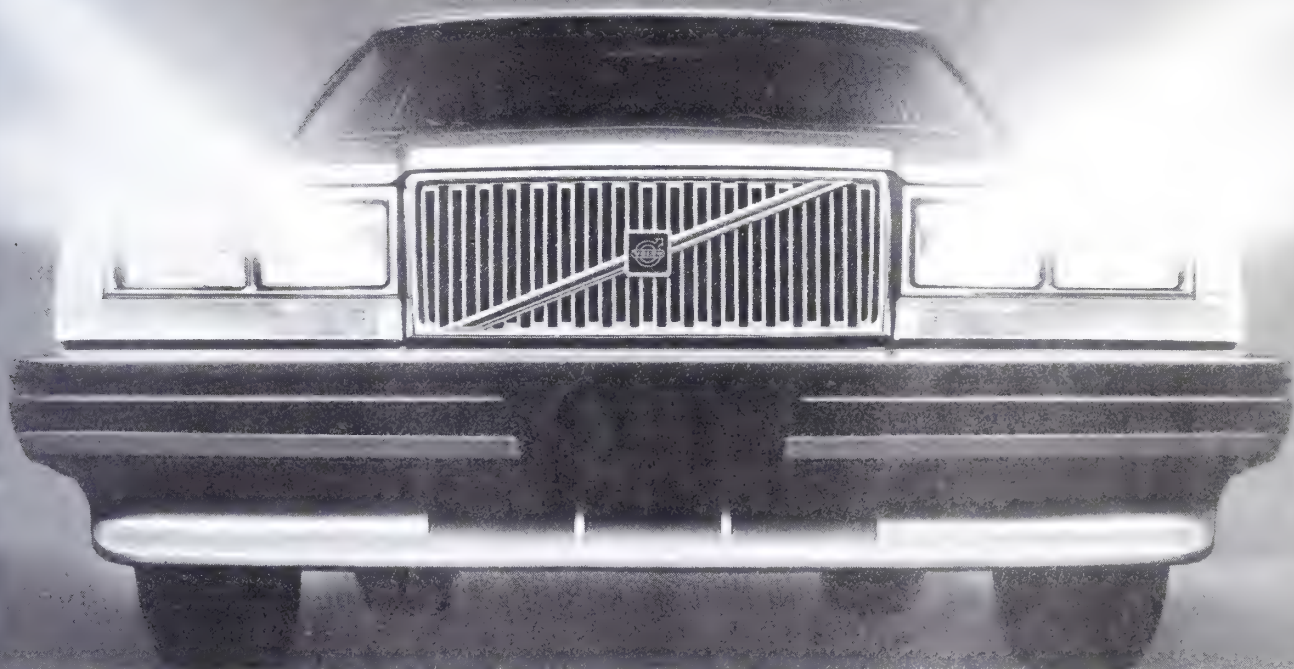
But the doomsayers may be way off base. Despite widespread expectations of labor shortages and higher wages, neither have come to pass. Nor are they likely to in 1989. Wage gains, far from driving up the price indexes, are barely keeping pace with rising prices. Even more important, the economy shows no sign of running out of workers. Today, it seems, labor demand is creating its own supply, bringing new workers into the market. In January alone, the labor force—those who are employed or seeking employment—increased by a staggering 870,000. Seasonal factors may have exaggerated the gain, but it is impressive nonetheless. Says Irwin L.

ployment was hit hard by the onslaught of imports. The press of foreign competition and the waning of union strength kept a lid on wages.

THE TEEN SECTOR. But over the past couple of years, as factories shifted into overtime and employment in other sectors continued to grow strongly, wages barely inched higher. Even in 1988, the conviction grew that employers would run into labor shortages, wages didn't rebound as expected. Real compensation per hour—which includes wages and benefits, adjusted for inflation—rose by a mere 0.6% last year. And even though real weekly earnings leaped in January, they had fallen in November and December.

True, wages are accelerating in some sectors of the economy, but that isn't too troubling. The shortage of teenage fast-food workers, for example, has pushed hourly salaries well above the minimum wage in some regions. Indeed,

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Economics

service sector wages and benefits on a
average rose 1.2% in 1988 after adjustin
for inflation. But rising wages in th
types of jobs that teenagers hold a
unlikely to trigger widespread inflation
By contrast, real wages and benefits
manufacturing—with its large comp
nies and more unionized work force,
rose just 0.2% in 1988.

Two demographic factors are spurring
the supply of labor and holding dow
wages. First, the baby-boom generatio
has moved into its prime working year
providing a hefty pool of labor for man
jobs. Second, women continue to ente
the labor market in record numbers. A
a result, the proportion of the adult po
ulation in the labor force—known as th
labor force participation rate—has rise
from 64% to 66.5% over the past seve
years (chart, page 90).

Since each percentage point repre
sents 1.85 million people, the rising pa
ticipation rate has been an importan
source of workers for the economy. I
1988, for example, if the labor force pa
ticipation rate had remained the sam
the influx of baby-boom workers wou
have added about 1.2 million adult wor
ers. But the labor force actually grew b
1.8 million people, reflecting an additi
al 600,000 women joining the labor fore

MOVING JOB MARKET. New workers al
not the only source of labor. There al
6.7 million unemployed workers and a
proximately 1 million "discourage
workers"—people who would want a jo
but who aren't looking because the
don't think they can get one. Many o
these people are in slow-growing region
of the country, but some are moving t
healthy states.

Over the past four years, Florida, fo
example, has been one of the fastest
growing states in the country, adding
new jobs at 4.8% annually. Yet its labo
force has grown almost as fast, accordi
ing to Rebecca Rust, an economic an
lyst in the Florida Labor Dept., becau
the buoyancy of the local economy a
tracts immigrants from other states
and countries.

Even in the industrial heartland, r
covering economies are pulling discou
aged workers back into the work fore
In Michigan, the labor pool grew by 3.3
last year, far above the national averag
of 2%, in response to the new vigor
manufacturing. Likewise, in Pennsylv
nia, the labor force grew by 2.3%. Don
ald Loughery, chief of research an
analysis at the Pennsylvania Labor
Industry Dept., says he is "absolutel
certain that the growing economy
pulling people out to get a job." Lough
ery notes that there is still some room
grow, since there are counties in th
state with large numbers of discourag



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Economics

workers, keeping labor force participation rates lower than 50%.

The same principle holds on the national level. There are about 140 million people from age 20 to 64 in the U.S., and 30 million of them are neither employed nor looking for work. If there were unfilled jobs, how hard would it be to get some of these people to take them? Not all that hard, says John Heiman, economist at the Claremont Economics Institute. "People want to work. They don't have to be dragged kicking and screaming into jobs."

Of course, many economists remain unconvinced that the supply of workers is so ample. "We're running out of slack

**'People want to work.
They don't have to be
dragged kicking and
screaming into jobs'**

in the labor market," says Allen Sinai, chief economist at Boston Co. "We're at full capacity." Sinai and others acknowledge the existence of a large nonworking population, but they argue that these people don't work because they are mothers of small children, senior citizens, and hard-core "untrainables," who are not easy or cheap to hire.

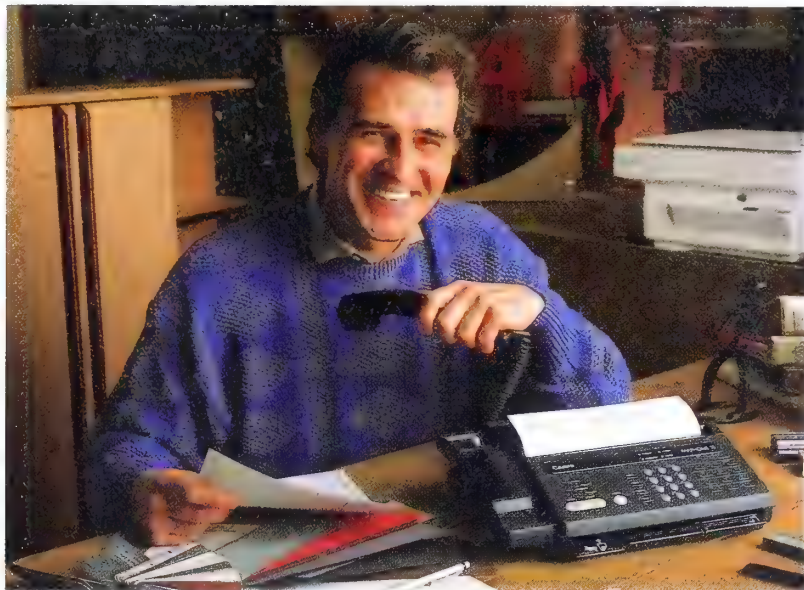
'NOTHING HAPPENED.' For these reasons, the reserves of unemployed and discouraged workers have almost been exhausted, argues Charles Lieberman, director of financial markets research at Manufacturers Hanover. According to his calculations, if the current rate of job growth continues, the economy will run out of easily employable workers by approximately the middle of the year, and labor costs will rise at a 6% to 7% annual rate by yearend.

Two years ago, when the unemployment rate was drifting down to 6%, economists were making the same arguments. Instead, says Richard S. Belton of the National Planning Assn., "it was like the dog that didn't bark in the night—nothing happened."

Now that unemployment has fallen to 5.4%, the same economists are back again issuing warnings. And just as before, people are ready to believe them. To be sure, 4 million people gained jobs in the past two years, and that means there are 4 million fewer individuals hunting for jobs. But with millions of Americans still out of the work force, it seems premature to bet that there's only one left to hire.

By Michael J. Mandel in New York

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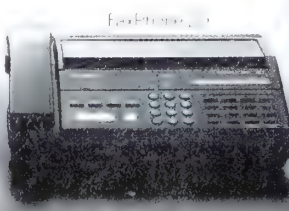
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THE TRILLION DOLLAR MAN

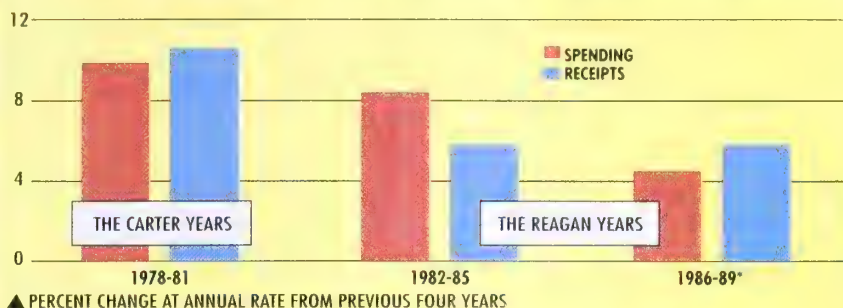
CAN RICHARD DARMAN TAME THE DEFICIT?

Wander into Room 252 of the Old Executive Office Building on a chilly Washington Saturday, and you're likely to be greeted by a startling apparition. There, in the spacious suite of the Director of the Office of Management & Budget, sits a disheveled figure who looks for all the world like a refugee from a nearby soup kitchen. He wears a tattered plaid sport coat with a ripped elbow. His loafers are worn out, his socks torn, his pants rumpled. To complete the look, there's the clashing electric blue polo shirt and do-it-yourself haircut. Could this be the Bush Administration's budget chief, the man with the trillion-dollar checkbook?

None other. Richard G. Darman, tapped by President Bush to lead the Administration out of the budget wilderness, seems strangely out of place with his preppier-than-thou brethren—even though he dons his seedy getup only on weekends. With the exception of Housing & Urban Development Secretary



WITH THE BUDGET GROWING MORE SLOWLY...

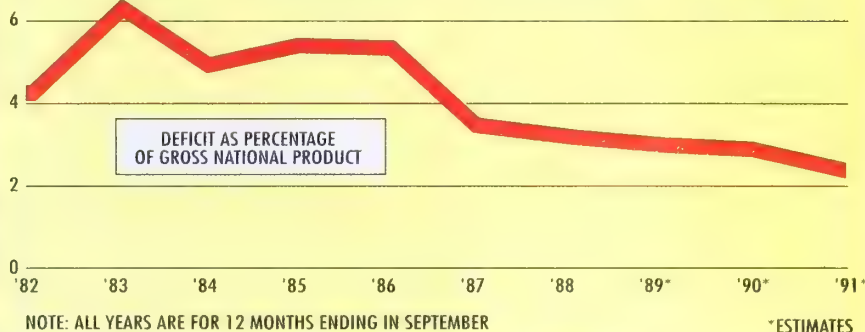


...BUSH IS RELYING ON HEFTIER TAX RECEIPTS...

	BUSH'S PROPOSED BUDGET (BILLIONS OF DOLLARS)			
	1988	1989*	1990*	1991*
OUTLAYS	\$1064	\$1149	\$1160	\$1211
PERCENT CHANGE	6.1%	8.0%	1.0%	4.4%
RECEIPTS	\$909	\$979	\$1066	\$1147
PERCENT CHANGE	6.4%	7.7%	8.9%	7.6%
DEFICIT	-155	-170	-94	-64



...TO LIGHTEN THE DEFICIT'S IMPACT



ick F. Kemp, most of Bush's Cabinet heads are good gray members of the establishment, not given to bold ideas or cat-rocking. Darman, the Bush team's resident policy guru and numbers-cruncher, is different.

Darman is an able strategist with a varying intellect—and an ego to match. He has what George Bush calls “the vision thing.” Darman's years at Harvard business school, the White House, and five government departments have revealed interests that extend far beyond the spreadsheets that usually attract budget directors. He's almost blasé about what many view as an awesome task: slashing the \$170 billion deficit. “We will succeed at deficit reduction,” he says. “But if that's all we do, we won't have done much.”

Under Darman, look for the OMB to become a kind of national think tank. The ideas are already tumbling out, from the cosmic to the half-baked. As popularizer of the word “corpocracy” to

describe bloated and bureaucratic corporations, Darman dreams of supplanting the Me Generation's fixation on short-term profit and instant gratification with a new, future-oriented ethic (page 102). His ideas are behind many of President Bush's recent sermons on the subject. But beyond fervent expressions of concern, Darman hasn't yet figured out how the government can shift the nation's time horizons to the longer term. He's working on it.

RED SEA. Darman has a couple of priorities, though. One is revamping the Pentagon's cumbersome and expensive contracting system. Bush has promised to implement the 1986 recommendations of a blue-ribbon panel headed by industrialist David Packard. Ronald Reagan largely ignored Packard's proposal that more weapons-buying power be given to top Pentagon civilians, rather than individual services. By helping to put the reforms in place, Darman could free precious funds for other initiatives.

Darman also would like to stiffen teaching standards, though that's mainly the province of state and local government. But he feels Washington can give the states direction. He has already asked top scientists and engineers for advice on ways to beef up basic math and science skills. And he dreams of overhauling a health care system that is crumbling under the strain of a growing elderly population. “I want to restructure the budget to call attention to some of these long-term issues,” Darman says, tugging on a fraying sleeve.

That's ambitious stuff, even for a 45-year-old whiz kid. But George Bush has a lot riding on his young budget chief's success. Darman's wish list, however vague, is the closest thing the Bush Administration has to a domestic agenda. If the President is to keep his promise of a “kinder, gentler nation,” Darman will have to turn campaign rhetoric into reality—on a shoestring. Failure would leave the Administration adrift in Rea-

gan's sea of red ink. Success, Darman knows, would make him one of the most influential budget directors in history.

Despite its reputation as a haven for bean-counters, the OMB is the perfect spot for an ambitious policy junkie like Darman. Virtually every domestic initiative passes through his office. The OMB also mediates conflicts between departments, approves congressional testimony, and reviews federal regulations. But before he can use these levers of power to push his broader agenda, Darman must end Washington's fixation on the deficit. As a starting point, he will have to forge credible agreements with Congress to comply with the Gramm-Rud-

man Act. Although it's far from watertight, the law triggers across-the-board cuts if Congress and the Administration can't get the deficit down to \$110 billion for fiscal 1990.

It will be ticklish. The Congressional Budget Office estimates that without changes in current spending programs, next year's deficit will be \$141 billion. Simply plugging in rosier assumptions on interest rates and economic growth, as the Reagan Administration did, whittles the projected deficit down to \$127 billion. So if the White House and Congress want to reach an agreement, they have to find only \$17 billion in savings in a \$1.2 trillion budget. That may be small

change by Washington standards. But because the budget struggle is a crucial test of wills between Congress and President Bush, a tortuous path lies ahead.

To begin the process, Darman drew up a budget of almost Machiavellian design (page 103). He threw out the notion of baselines, for example: Instead of comparing proposed spending level with the cost of maintaining current programs, Darman measured Bush's proposals against actual 1989 spending. In the case of Medicare, the move allowed Bush to claim that spending will increase by \$8 billion. In fact, his budget would cut by \$5 billion the amount needed to maintain current services.

BACKHANDED SALUTES. To many, that smacks of smoke and mirrors. "It's like starting to count touchdowns in the middle of a basketball game," complains Hill budget aide. "We've got the Phantom of the Budget," fumed Senator Ernest F. Hollings (D-S.C.) during a recent hearing. He complained that Darman is "more Jack-be-nimble than [predecessor David] Stockman."

But to an inveterate schemer like Darman, who approaches negotiations by "multiple-contingency planning," such grumblings are compliments on skill honed in a government career that dates back to the Nixon Administration. Now he is trying to persuade wary congressional Democrats to join in a high-stakes negotiation to bring the deficit down on George Bush's terms. "When it comes to designing a process that gets you to a desired agreement, there's no one better than Darman," says Craig I. Fuller, a lobbyist and former top Bush adviser. Some key elements of the Darman method:

■ **The buddy system.** A believer in bipartisanship, Darman has asked Hill Democrats to become partners in the budget process. That's partly a recognition of Bush's limited leverage over the Democratic Congress and partly a reflection of Darman's distaste for the confrontational approach that dealt Reagan out of the budget game after 1982.

The pacific overtures have paid off some. "There is a difference with Darman," says Senate Budget Committee Chairman James R. Sasser (D-Tenn.). "The White House is being less rigid." Adds Fuller: "It's important that the Bush budget be kept in play. Dick has managed that very well."

■ **Diversionary tactics.** Like a pilot starting a bombing run, Darman likes to confuse the opposition's radar with a cloud of chaff. "It's desirable to have a few distractions in the early phase," he says with a grin. By coming up with what congressmen call a "black box" of some \$10 billion in unspecified spending cuts

THE DARMAN DIET FOR BLOATED BUSINESSES

In late 1986, shortly before resigning his Treasury Dept. post to join Shearson Lehman Hutton Inc., Richard G. Darman gave a controversial speech in which he blasted the "bloated, risk-averse, inefficient, and unimaginative" management of U.S. business. His attack on what he called the corpocracy made headlines around the country.

A lot has happened since then—both to Corporate America and to Darman. Merger mania and the slew of leveraged buyouts have changed the face of U.S. business. Profits from the wave of transactions also allowed Shearson to pay Darman nearly \$2 million for a 20-month stint as a managing director.

Now that he's back in government, Darman has muted his rhetoric a bit. But his fundamental criticism is just as harsh. "We have a societywide value problem," he says. "The energy of our best people is going into financial paper-shuffling." That tendency, Darman complains, results in a focus on short-term profits at the expense of such long-term concerns as improved quality and manufacturing prowess.

Darman sees advantages in some aspects of what might be considered paper-shuffling, however. Unlike some of his Administration colleagues, he believes that takeovers inject some needed discipline into the system: "The threat and reality of takeovers has forced managers to attend more to costs and hidden value that is not adequately reflected in stock price."

Likewise, he says, the rise of ambitious, bottom-line-oriented managers generally has been for the best: "The infusion of young people entering management at very high levels serves to shake up the old order." He shrugs off the worries of some analysts that because these mobile Young Turks have no corporate loyalty, they never look beyond the next earnings report.

'MORAL MATTER.' Darman doesn't think that the changes have gone far enough, however. Old-line manufacturing companies show signs of getting tougher, he believes—but the fast-growing service industry does not. "A whole lot of the service sector remains highly inefficient and vulnerable," he says.

Darman's list of suggested solutions includes tax breaks for research and development and new incentives to encourage business to use equity financing rather than debt. He also seeks major improvements in education. "We need much more investment in human capital," he says.

Don't look for gobs of money from Uncle Sam, though: Darman believes that subsidies and the like "can only help marginally." The key, he argues, is a fundamental shift in national thinking. "We've got to change the system so that society attends more to the future," Darman insists. "It's more a moral matter than one of financial incentives." That means you can watch for more sermonizing from Darman.

By Howard Gleckman in Washington

cor-poc-ra-cy *n.* An inefficient, unimaginative, risk-averse corporate management that has acquired the worst characteristics of the government bureaucracy

Darman has bought time to feel out the opposition. He also has focused the opening debate where he wants it: on the process and away from defense cuts and tax hikes.

Pressure points. Darman knows that nothing happens in Washington without a crisis or the threat of one. If budget negotiations are dragging in late summer, two deadlines could move a deal along.

Sometime, probably in September, the government will exhaust its borrowing authority. Lawmakers will be acutely embarrassed if they must raise the debt ceiling without agreeing on modest deficit reductions. Darman could use that pressure to keep talks on track.

If that isn't enough of a prod, Gramm-Rudman's automatic 10% spending cuts will kick in on Oct. 15. Darman is threatening to use the meat-ax if Democrats insist on higher taxes.

The ultimate threat is the one of instability in the financial sector. Although the markets haven't paid much attention to the budget drama lately, they are already edgy over rising interest rates. If rates continue to climb and traders sense that budget talks are going badly, the impasse could send Wall Street into tailspin. Such market pressure led to budget agreements in 1982 and 1987.

Flexibility. With the exception of major



RICHARD GORDON DARMAN

Born: May 10, 1943, in Charlotte, N.C.
Prepared at Rivers Country Day School.
Home Address: 139 Abbott Rd., Wellesley Hills, Mass. Field of Concentration: Government.

HARVARD MAN: IS HE "MORE JACK-BE-NIMBLE THAN STOCKMAN"?

tax increases, Darman has put the whole budget up for negotiation. Bush's opening bid on military expenditures, for instance, holds spending growth only to the rate of inflation. Administration officials hint that they could accept even less. That would allow Darman to give up ground to Democrats, who could claim a victory by adding money for domestic programs.

Bush appears dead set against new taxes. But no one will be surprised if he eventually agrees to a budget deal that contains a few billion in new revenues. By floating a controversial proposal to bail out the savings and loan insurance fund through a tax on deposits, the Administration has shown itself to be remarkably fluid in its definition of acceptable "user fees."

Indeed, Bush weighs his words carefully these days when talking about his vow to oppose new taxes. Asked whether he intends the pledge to be in place for four years, Bush says: "I'd like it to

be." The implicit message: If Democrats cut spending now, he may agree to some device to raise new revenues if they're needed to balance the budget in the future.

Although Darman is a compulsive planner, he isn't sure what shape the final deal will take. He's only certain that there will be a "grand compromise," much as there was with the 1983 Social Security package and the 1986 tax reform bill—two other big negotiations that he helped direct. In the end, he says, it will all come down to "the chemistry of the negotiating process. Opportunities will open. You seize them."

'YOUNG ROMANTIC.' Darman has been seizing opportunities most of his life. An intensely private man, he can spend hours spinning out his ideas, his eyes dancing and his hands furiously doodling on a notepad. But when the talk turns to personal matters, he turns introspective, shrinking into a chair and nervously crushing a soft-drink can.

He has always been surrounded by powerful men and torn by conflicting forces. Born into a family of wealthy New England mill owners, he pushed himself to meet his elders' high expectations. His grandfather, Arthur, was a Russian immigrant who made a fortune from wool mills in Woonsocket, R.I. Darman's father, Morton, was a savvy

BUDGET POKER: HOW DARMAN STACKS THE DECK

Just how big is the deficit in George Bush's 1990 budget? He says it's \$94 billion. Or is it more like \$120 billion? Much of the difference lies in some sleight of hand by Budget Director Richard G. Darman in estimating spending. For example:



THE INTEREST RATE FINESSE

The Bush budget assumes that short-term interest rates, now 8.7%, will plunge soon and reach 6.5% by the end of the year. Most economists think a drop in rates is wishful thinking. If interest rates simply stay where they are, spending could be some \$9 billion higher than the levels projected in Bush's budget.



THE BLACK BOX

Darman has assumed that nonmilitary spending will be reduced by \$10 billion or more in 1990. Where will the savings come from? He didn't say. Irritated legislators complain that the move will let the Bush Administration take credit for spending increases, while Congress takes the heat for spending cuts.



THE BASELINE SHUFFLE

What Washington calls "cuts" in the budget are really reductions from what spending would be if no action were taken—the "baseline," in budget speak. Some Darman cuts are measured from Ronald Reagan's proposed 1990 budget, others from current law. Congress is still trying to sort out the impact on the deficit.



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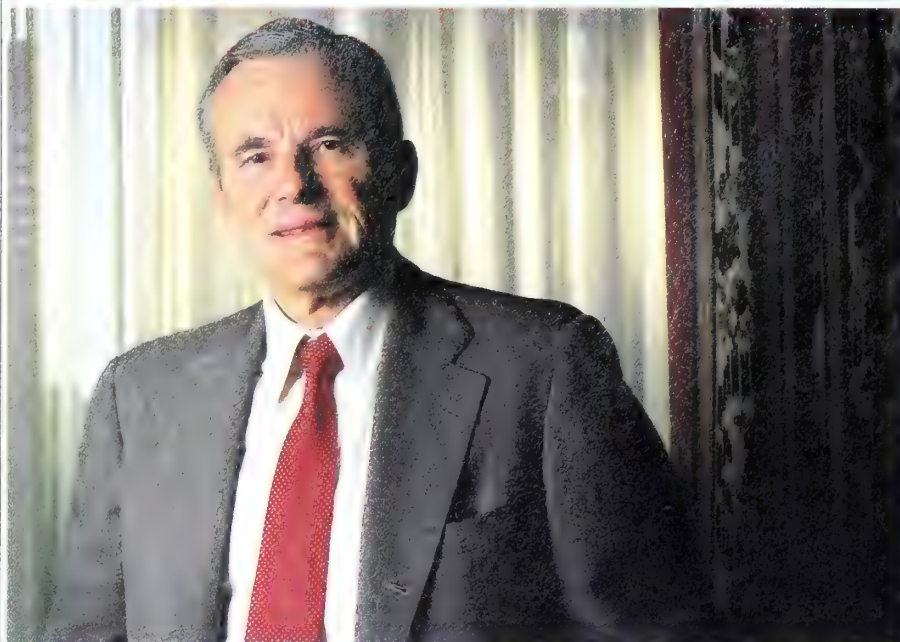
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BRADY: A FALSE START AT TREASURY—BUT HIS CLOSE TIES TO BUSH MAY GIVE DARMAN TROUBLE

businessman who diversified the family holdings out of a dying industry into real estate and other interests. Both men were "extreme perfectionists," Darman says. "There's a little of that in me, too."

Darman grew up a long way from Woonsocket, in the well-to-do Boston suburb of Wellesley Hills. Early on, he chafed at the idea of taking over the family business. He was more attracted to his mother's notion of social obligation: She did volunteer work with terminal cancer patients and the needy. By the time he was 13, Darman recalls, he was telling schoolmates that he expected to tackle the nation's problems as a Cabinet officer some day. "I was a young romantic," says the man who is known today as the ultimate pragmatist.

OLYMPIC EFFORT. At Harvard in the early 1960s, he got caught up in John F. Kennedy's soaring rhetoric, despite the Darman clan's Republican lineage. Even today, Darman will quote long passages of J.F.K.'s inaugural address. On his office wall is a college yearbook photo of Kennedy addressing Harvard students.

Kennedy's call to public service stuck with Darman. But he didn't react, as some of his classmates did, by signing up for a tour of duty with the Peace Corps in Peru. Instead, Darman put his reformist impulses on hold while he earned an MBA at Harvard. This curious blend of idealism and practicality marks Darman to this day. "He wasn't dreaming of making bucks like everyone else," says Walter Channing, a B-school classmate. "He was more interested in power and influence and getting things done."

Darman's penchant for playing the angles also showed up early. Channing re-

members that Darman suddenly took up biking, entranced by the notion of making the U.S. Olympic bicycle team. It wasn't just out of love of the sport. Channing says that Darman researched the U.S. Olympic teams and deduced that his odds of success were highest on the bicycle squad, which had a dismal record. "The weakness in the field intrigued him," Channing says. Darman, who abandoned the effort after a few months of training, dismisses the episode as a youthful lark.

Darman's fling with the world of commerce lasted about as long as his cycling days. After B-school, he was offered a job at McKinsey & Co. It was a dream job for most Harvard MBAs, but Darman quit after a summer. Management consulting, he says, was little more than "designing boxes without a lot of thought about what goes into them."

Performing much the same chore for the Washington bureaucracy was something else, however. Darman was one of a group of Harvard MBAs who signed on as systems analysts for the Health, Education & Welfare Dept. At HEW he met Elliot L. Richardson, an archetypal high-caste, good-government Republican who embodied Darman's public service ideal. Darman became a Richardson protégé, fol-

lowing him through HEW, the Defense Dept., and the Justice Dept. in the Nixon Administration. The whirlwind tour ended abruptly in October, 1973, when Attorney General Richardson was fired in the Watergate Saturday Night Massacre. Darman was among the aides who followed Richardson out the door.

BAKER'S MAN. The experience helped cement a close bond between the two men. "Elliot Richardson was an enormous influence on my life," says Darman. "He was a mentor in the best sense." Despite the pair's wealth and pedigree, Darman says that Establishment blue bloods still regard him and Richardson as interlopers. Among other things, Richardson taught his young pupil that government is a noble career, but success depends on learning to be a skilled infighter.

After leaving Justice, Darman dabbled in consulting with some former Harvard buddies and did a stint as a Wilson scholar. In 1976 he was back in government, serving as an Assistant Secretary in the Commerce Dept. That's where he encountered James A. Baker III, an astute Texas politician who was to give Darman's career its second boost. Joining the White House staff as Baker's deputy in 1981, Darman quickly established himself as a power in his own right. Four years later he followed Baker to the Treasury Dept., where he served as Deputy Secretary.

By the time a bored Darman left Treasury in 1987 to be a managing director of Shearson Lehman Hutton Inc., he was known as a wheeler-dealer. His most fabled move was striking a pact with Stockman in 1981 to push for the largest tax cut in history—although they knew that the bill would be a budget-buster. Within months, Darman was plotting a tax hike to undo the damage.

Such moves helped earn him the enmity of a large group of detractors who felt betrayed by his deviousness and scorched by his arrogance. That could complicate Darman's efforts to forge a budget compromise. "Darman's reading Bush's lips so far," says one former top White House aide. "But how long will he stay a born-again conservative?" Darman also suspect on Capitol Hill, where House Ways & Means Committee Chairman Dan Rostenkowski (D-Ill.) was only one of the



SUNUNU: WORRIED THAT HE'LL BE LEFT OUT OF THE BUDGET PROCESS



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Cover Story

legislators who did battle with him. Darman concedes that he may have stepped on too many toes in the Reagan years and ascribes some of his earlier hauteur to "immaturity." Since landing the OMB job, he has spent hours courting key legislators. Lawmakers, including Rostenkowski, say Darman really has seemed to mellow.

Darman says that his wife, Kathleen, is responsible for "much of the 'kindergentler Darman.'" She is a cultural historian who spends most of her time researching and writing—and avoiding the Washington social whirl.

He is staying on his best behavior when it comes to fellow Administration heavyweights. Both Treasury Secretary Nicholas F. Brady and White House Chief of Staff John H. Sununu will be major players in domestic policy. Darman will have to tread carefully around both men.

HIRED HAND. Brady has had problems settling into his job, and some Washington cognoscenti are dismissing him as out of his depth at Treasury. Darman, who has the fiscal policy expertise that Brady lacks, may be tempted to fill the vacuum. But Darman's intellectual cadlepower may prove no match for the old school tie: Brady is a longtime Bush intimate, while Darman is, in a sense, a hired hand to whom Bush has no personal loyalty. "Dick's been very careful," says a White House insider. "He's smart enough to know that he can't get on Brady's wrong side."

Another potential conflict looms with Sununu. Like Darman, the Chief of Staff is brainy, volatile, and used to getting his way. The big difference is philosophical: Darman is at heart a reformer who believes the federal government has an important role to play. Sununu is a bedrock conservative of the New Hampshire school. Sooner or later, Bush aides fear, the two headstrong men will clash. Says one GOP official: "Sununu's concern is that Dick will run off and do a budget deal without him." Already, Sununu aides are eyeing the peripatetic Darman nervously. "Dick Darman is not the budget czar," huffs one. "He's the budget director."

You couldn't tell by listening to the man in the ragged sport coat. "We've got to change the system so that society attends more to the future," says Darman. "There's a whole series of things I'm going to pull together under that heading, and what'll be in there, I don't yet know. But I know this: We've got to invest our intellectual capital better. And as soon as he gets this trillion-dollar budget thing under control...."

By Howard Gleckman, with Lee W. Czark, in Washington

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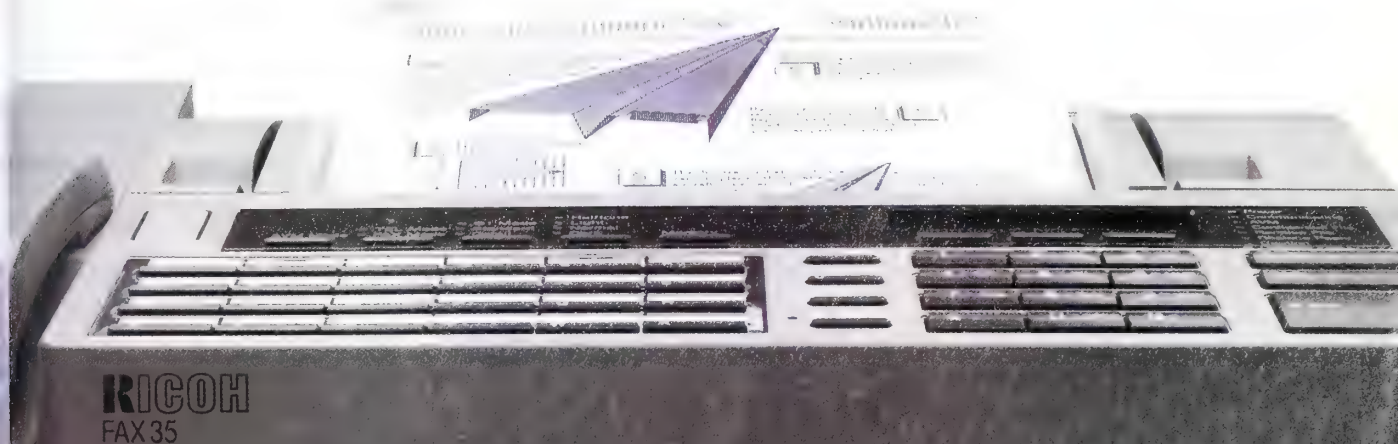
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MILES OF AISLES: BRAND NAMES AND SPECIALIZED 'SUPERSTORES' ARE IN—PROMOTIONS ARE OUT

Tom Jones struts down the nearly empty aisles of Sears, Roebuck & Co.'s Schaumburg (Ill.) store like a proud new father. As the store manager surveys his domain, scores of workers quietly re-tag tens of thousands of items and string up banners trumpeting Sears' new "everyday low prices." Suddenly, passing the hardware department, Jones stumbles upon a forgotten yellow sign announcing an old sale—a no-no in Sears' new world of one-price retailing. "There are a few of these yellow cards still around," says the 21-year Sears veteran as he pulls it out of sight, "but by midnight, there won't be any left."

If only the problems at Sears' huge \$30.3 billion retail business could be so easily erased. America's Big Store is in big trouble. Once the keystone of U.S. retailing, Sears' network of general-merchandise stores no longer holds sway in the industry. Trendier specialty retailers and superdiscounters have siphoned off consumers and market share during the past decade. And Wall Street has repeatedly bashed the retailing colossus for its bloated costs and lackluster earnings.

Now, in a sweeping bid to lure back shoppers, Sears on Mar. 1 unveiled its

new one-price strategy. Following a 42-hour national shutdown of its 824 stores to re-price some 50,000 items, Sears reopened for business with price reductions of up to 50% (table). To get the word out, Sears launched a dramatic media blitz, airing more than 2,000 TV and radio spots and running 900 newspaper ads over a three-week period. "This for us is a marketing revolution, and to trickle it out diminishes the effect on the customer," explains Michael Bozic, chairman of Sears' merchandise group.

Just how much of a revolution remains to be seen. But you can't accuse Bozic of thinking small. His grand strat-

egy is to permanently markdown items from current levels and run fewer sales promotions. Besides luring more value-hungry customers, Sears executives hope to ring up big savings of their own. While Sears managers don't expect a revenue bonanza, those old sales were expensive to run. With fewer such promotions, Bozic believes Sears will in time save \$20 million a year in advertising and inventory-handling costs.

MARKET SLIDE. Still, Bozic's strategy has big risks. After decades of conditioning consumers to hold out for frequent off-price sales, Sears may confuse shoppers with its overnight change. And by making its pricing more predictable, Sears could find itself an easy mark for lower-

cost rivals. But the real question is whether Sears is committing itself to rock-bottom pricing strategy before reeling in its runaway costs. Sears' selling and administrative expenses gobbled up 30¢ of each sales dollar last year—compared with an estimated 23¢ at Kmart Corp. and a mere 20¢ at hardware superstore Home Depot. And despite belt-tightening, Sears' costs grew faster than sales in each of the past five years.

Rival Montgomery Ward & Co., on the other hand, reduced costs by 5% over the last three years before introducing everyday low prices in most departments last month. "The cost issue is the most significant in a one-price strategy," notes Bernard F. Brennan, Ward's chairman and the brother of Sears Chairman Edward A. Brennan. Adds a former Sears executive: "In order to be successful with everyday low pricing, you have to have everyday low costs."

But Bozic can't afford to wait. Sears' market share has slid 33% over the past decade, and Wall Street has grown increasingly displeased with its lackluster returns. Nor have investors been thrilled by management's glacial pace in getting its store in order. Sears' stock has

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DATA: SEARS, ROEBUCK & CO.

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ruce Sobolov of CBS News, Laura Gismondi and Bruce Goldberg, AT&T, savor the afterglow of their own post-election victory. They take us behind the scenes for a glimpse at some of the reasons why CBS was successful on election night.

FEBRUARY 15, 1989

AT&T: Afterwards, the critics said CBS was the best, the fastest.

CBS: Right, but we sweated it out for more than a year. With more 20-hour days than I care to remember.

AT&T: Your situation was pretty complicated.

CBS: We were faced with election projections, exit-poll analysis, and other studio programming applications running on IBM hosts.

AT&T: Plus the NewStar system we tied in with our wide-area network, ISN. It's distributed networked computing. Hey, we thrive on this stuff.

CBS: We're impatient around here. Speed is the only way you succeed with election coverage. The first thing we did was provide multi-host access with the 6500 System. Last election, everybody who needed access to voice systems used two terminals. Twice the space, twice the cable, additional controllers, added expense, and wasted time.

We had programmers working simultaneously on three host applications, two bisync, one SDLC. They were constantly skating between terminals, wearing ruts in the rug. Now they have access to multiple sessions simultaneously from one terminal.

AT&T: The data moves over twisted pair, the same type wiring the technicians pulled for your System 75 PBX. That made sense.

CBS: An added advantage was having the same dedicated AT&T technicians installing and maintaining our system, providing consistency to my operation.

AT&T: But really, Bruce, why us?

CBS: Your responsiveness. At

Skating between terminals put ruts in the rug.

CBS, we all agreed that what we needed was someone who could deliver it fast, install it, test it, and support it. And you were hungry. You never said, "No, we can't do it." And you never took long to say "yes."

AT&T: You had computer networking problems. Solving them is the house specialty.

CBS: We do distributed computing to the nth degree. Our reporters are all over the country. They call in their results when the precinct closes. Before, we had over a hundred operators standing by, with phones and terminals. That election night we introduced the voice response system running on AT&T PCs.

AT&T: How many calls?

CBS: Thirty, thirty-two calls at once, reporters everywhere having voice response conversations with the IBM host. And all done with the same

custom host software we always used. We greatly reduced our cost.

AT&T: The other networks are watching, thinking, "How come CBS has the results already and we don't?"

CBS: It was a good night for us. Now the name of the game is streamlining for 1990. We're talking about a networked computer solution as a gateway into different host systems.

AT&T: With the AT&T Systems already up, running, and in place, we can almost completely automate your survey system.

CBS: That's a real big plus for all of us.

AT&T: Something tells me I've seen that same glint in your eye before. (Laughter)

The CBS Solution:

THE CHALLENGE:

Integrate IBM and DEC host computers and NewStar editorial system. Build an advanced computerized voice response system to speed election-night projections.

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THE RESULT:

CBS News provided fast, accurate election coverage throughout Campaign '88. The *Baltimore Sun* reported that, "CBS was recording results in all sorts of key races faster and with far more authority than either of the other networks."

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scarcely budgeted in five years, while high-flying Wal-Mart Stores Inc.'s share price has nearly quadrupled.

For years, many believed Sears was protected from a raider by sheer size: Its current market value is \$15.6 billion. But now even Sears may be looking over its shoulder. The \$25 billion takeover of RJR Nabisco Inc. has shown that no target is too large for a hostile buyout—especially a highly visible laggard such as Sears. "The securities marketplace is saying, 'We are impatient, and we have a way of dealing with underperformance,'" says Sidney Doolittle, president of retailing consultant McMillan-Doolittle.

BRAND NAMES. Last October, after Sears' stock price jumped on takeover rumors, Brennan announced a restructuring that included the \$1.6 billion buyback of 10% of Sears shares and the sale of the 110-story Sears Tower. He also placed parts of Sears' Coldwell Banker Real Estate Group and Allstate Insurance Co. units on the block.

But perhaps the most difficult part of the plan will be Bozic's makeover of Sears' troubled retailing business. The new everyday low pricing strategy is only the start. After years of relying on a stable of private-label products such as Kenmore washers and Craftsman tools, Sears is adding more brand-name goods. Part of Sears' media blitz highlights the 1,000 name brands already sold at Sears—with new brands being added each week. At the Schaumburg store, for instance, signs hawking Oshkosh B'Gosh overalls beckon shoppers to the store's new work-clothing department. And a banner above the electronics boutique promotes Sony and RCA gear alongside Sears' little-known LXI brand.

Meanwhile, Bozic is trying to make Sears into a collection of specialized "superstores"—a strategy already embraced by Ward. By yearend, Bozic will open new Brand Central appliance and electronics superstores within 400 stores. And he wants to debut freestanding children's apparel and automotive superstores. "The more we behave like a competitor," says Bozic, "the better we compete like a competitor."

These changes will take time, though. Meanwhile, competitors aren't exactly running for cover. "Our policy has been everyday low pricing for the last 27 years," sniffs Teri Kula, marketing coordinator at K mart. And Wal-Mart Director Robert Kahn argues size and costs will prevent Sears from quickly remaking itself. "The laws of physics are against it," he says. Indeed, turning Sears' ponderous retail operation around may be as difficult as defying gravity.

By James E. Ellis and Brian Bremner in Chicago, with Michael O'neal in New York

AIRLINES

PHOENIX AIRLINES MAY GET ITS WINGS CLIPPED

The carrier pays big money if a jury verdict is not reversed

Michael J. Brady was flying high. He founded his own commuter airline in 1985 when he was only 36. By the end of last year his Phoenix Airline Services Inc. was a respected commuter carrier with revenues of about \$75 million. Operating as part of Northwest Airlin, Phoenix hauled 1 million travelers annually between Northwest Airlines Inc.'s hub cities, such as Minneapolis, and tiny nearby hamlets.

But Brady's great American dream

to testimony, Brady began trying to set up a similar operation for another major carrier. Witnesses testified that he even brought Trans World Airlines Inc. representatives on a tour of Metro's Atlanta operation and flew them for free on Metro planes—unbeknownst to Metro board.

The jury reached the conclusion that Brady was building an airline of his own. TWA officials testified that in December, 1984, they were startled to find that Brady's proposal came from his

newly formed Phoenix Airline—not Metro. TWA broke off talks. But Brady scored within weeks, landing a deal with Republic Airlines Inc., which was later acquired by Northwest.

Brady declined BUSINESS WEEK's requests for interviews. In court, however, he said he resigned from Metro on Dec. 21, 1984, and didn't officially incorporate Phoenix until the following Feb. 1. Brady also argued that Metro's tight finances and existing commitments with Republic competitors would have prohibited it from serving Phoenix' Northwest Airlines markets anyway.

But according to testimony by Metro officials, Brady did not quit until Jan. 8—after he had effectively established Phoenix Airline. Moreover, Metro blames Brady for luring its chief of maintenance and other key executives to Phoenix, which delayed federal clearance for some of its new aircraft to fly. "He really did betray us," says Metro President J. L. Seaborn.

Jurors apparently agreed, returning a guilty verdict that included punitive damages of \$5 million against Brady and a combined \$110,000 against two other Metro-turned-Phoenix officers. Barring a reversal, Brady's prospects are dim. Phoenix has few hard assets of its own to sell to satisfy the award. Metro, which values Phoenix at \$57 million and a going concern, may buy what's left of the company after the award is settled. If that happens, Brady and his crew could be grounded for good.

By Dean Foust in Atlanta



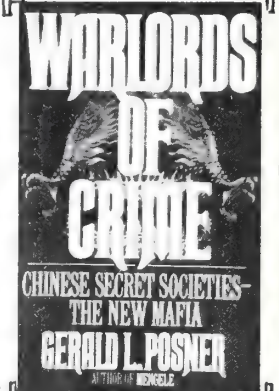
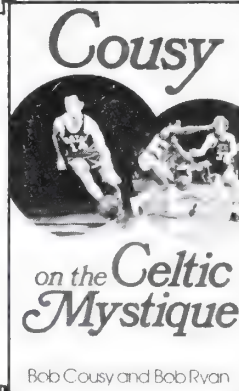
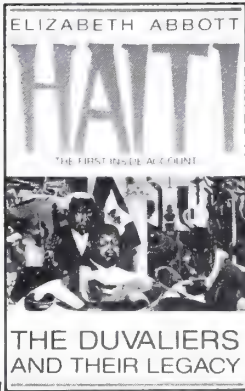
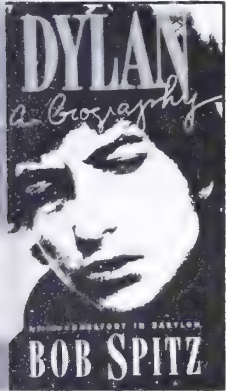
DID BRADY FOUND HIS COMPANY ON STOLEN BUSINESS?

has turned into a nightmare. A jury in Georgia's Fulton County Superior Court recently returned a hefty \$35.1 million judgment against Phoenix, Brady, and two other executives. The jury ruled that Brady and his managers had created their company by stealing a business opportunity from their former employer, Dallas-based Metro Airlines Inc. Brady's lawyers have appealed the verdict and a new hearing is set for March. If the award is upheld, however, Brady's tiny empire could come crashing down.

FREE RIDES. Court testimony tells a story of soaring ambition. After joining Eastern Air Lines Inc. in 1972, Brady moved quickly up the ranks of the company's operations side. He joined Dallas-based Metro in 1983 after a brief stint at another commuter airline. His troubles began one year later, when he went to Atlanta to help launch a Metro commuter service for Eastern flights. According

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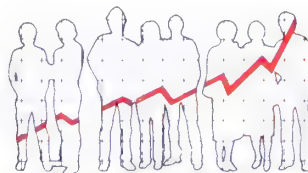
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FOOTE CONE CAN'T AFFORD NOT TO GAMBLE

's selling a thriving unit and looking overseas for growth

It's remarkable what a hungry ad agency will do. Executives at Foote, Cone & Belding Communications Inc. wanted a shot at the \$200 million Burger King Corp. business. Although the account isn't up for grabs right now, Burger King's new parent, Grand Metropolitan PLC, is looking to improve the struggling chain's marketing. Double was, the biggest account at B's public relations unit, Golin/Harris Communications, is Burger King's archrival, McDonald's Corp.—and that spells client content in capital letters. No problem: Feb. 23, FCB sold the PR unit to Britain's Shandwick PLC for an undisclosed amount.

Selling a thriving subsidiary to get a crack at a new account may not be like a long shot, but it's only FCB's latest gamble. On Jan. 24, the 13th-largest U.S. ad agency completed plans to merge its European operations with French advertising giant Publicis. Already, a \$2.8 million restructuring charge associated with the international expansion contributed to a 6% drop in FCB's 1988 earnings, to \$7.7 million on revenues of \$386 million.

The Chicago-based ad agency has little alternative to taking a few gambles. Despite FCB's long creative reputation, built on such campaigns as the California Raisins and Levi's 501 jeans, it hasn't been able to win any flashy domestic accounts recently. Worse, FCB has suffered several painful client losses and has been turning in erratic earnings for years. Last year, FCB's direct-marketing unit, Krupp-Taylor, lost its largest account, Home Shopping Network Inc., which had contributed about 25% of its revenues. Then client defections hit the agency, including the \$15 million Long John Silver's Inc. account and the \$10 million Frito-Lay Inc. account. FCB did not act enough new business from existing clients to make up for the losses, but it saw growth in U.S. ad spending slowly. FCB can't count on domestic accounts to fuel its future growth.

That's why FCB Chairman Norman W. Brown sees the booming overseas markets as a way to stabilize his company's performance. Publicis and FCB have formed a new Paris-based agency called Publicis-FCB, now Europe's second-largest ad agency network, with combined

And Publicis-FCB will enjoy a leading position in Italy and rank No. 3 in Spain. "It's a smart move giving each agency new areas of strength," says Tim Pollak, chief executive of HDM, a competing international venture owned by Young & Rubicam, France's Havas, and Japan's Dentsu. The agency will also have an advantage in media buying, says FCB President Abbott C. Jones. "There's more of an auction buying system in Europe, and we needed more media leverage for our clients," he says.

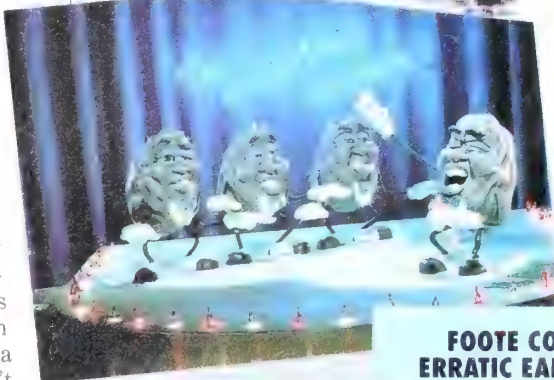
PERILS. This year, Publicis-FCB will contribute about \$10 million to Foote Cone's bottom line, estimates Merrill Lynch & Co., compared with \$3.5 million in earnings, excluding nonrecurring gains, produced by FCB's international operations last year. Already the partnership has snagged the \$20 million Philips appliance account.

Still, there are perils. The big challenge will be to meld corporate cultures into an effective agency. FCB's track record in this area isn't encouraging. Its 1984 acquisition of NCK Organization Ltd., a European advertising network, required a large amount of write-offs to cover the administrative costs of bringing the new agencies under the FCB umbrella. "They've had some past problems with strategic alliances," says Greg Ostroff, an analyst with Goldman, Sachs & Co. Merrill Lynch has lowered its 1989 earnings estimates 12%, to \$21 million, because of FCB's domestic headaches and possible further costs for the Publicis deal.

Even so, the European venture gives FCB an avenue of escape from the slow-growth U.S. ad business. Not so its sale of Golin/Harris, which comes at a time when other

U.S. agencies are rushing to diversify into PR, sales promotion, and other growing communications businesses. With such stable, lucrative clients as McDonald's, the PR subsidiary contributed about \$20 million of FCB's \$386 million in revenues last year. For its part, FCB says it didn't feel it could make the capital investments Golin/Harris needed to grow. But the agency has yet to put its erratic U.S. operations in order—and sacrificing a McDonald's in the hand for a Burger King in the bush seems like a risky way to start.

By Brian Bremner in Chicago with Pia Farrell in Paris



FOOTE CONE IS BEST KNOWN FOR ITS LEVI'S AND CALIFORNIA RAISINS CAMPAIGNS

billings of about \$2 billion. As part of the deal, FCB acquired a 26% stake in Publicis Communications, a new company formed to hold the French agency's advertising and media buying networks. Publicis gets a 20% chunk of FCB.

The deal should give Foote Cone more clout overseas. FCB's unprofitable operations in Britain will receive a boost from Publicis' two stronger agencies there.

FOOTE CONE'S ERRATIC EARNINGS



'ACE' GREENBERG TRIES TO TRADE UP

Can the onetime 'gunslinger' transform Bear Stearns into a world-class investment bank?

Gunslingers. That's what the Wall Street Establishment calls them. Tough, smart street-fighters who would just as soon pistol-whip you on a trade as look at you. That's the Bear Stearns bunch.

To the white-shoe crowd, these are the guys with an unsavory reputation that makes you want to count your fingers after you shake hands on a deal. This is a firm whose name surfaces when raiders get rapped by the government for parking and other violations.

Yet perception is not always reality, and the Street may have got it wrong this time. For one thing, while recent Wall Street scandals have brushed many of its clients, Bear, Stearns & Co. is one of the few houses still totally unscathed. "I'll tell you something that we're proud about," boasts Wichita-born Alan C. "Ace" Greenberg, chairman and boss of the Bear Stearns bunch. "We haven't received our first subpoena with regard to the stuff that's been going on in the last three years. Not one subpoena!"

'DOWNMARKET DREXEL?' The split between perception and reality is even greater when it comes down to business. Bear Stearns is seen as a small, blue-collar investment house (a "downmarket Drexel," sneers one critic) that makes its money in high-risk trading for wheeler-dealers and financings for the underprivileged of Corporate America.

Nothing could be further from the truth. Wall Street may be resting easy in its own contempt for the firm, but the Bear is emerging as a powerful money machine. It has a liquid, bulletproof balance sheet that is one of the strongest, most conservative on the Street. Quietly, Bear Stearns has grown to where it is now positioned to break into the select club reserved for those few investment houses that advise the biggest companies.

It is already picking up business lost by Drexel Burnham Lambert Inc., which stands accused by the

Securities & Exchange Commission of insider trading, securities fraud, and stock manipulation. Bally Manufacturing Corp., a longtime Drexel client, just switched to Bear Stearns—and other companies appear ready to follow.

But transforming itself from a trading house into a full-service investment bank won't be easy. The street is full of sad tales of trading firms self-destructing as they tried to do so. Lehman Brothers

lost its independence in a battle between traders and bankers. Salomon Brothers Inc., a trading powerhouse, is bleeding its best people in a similar fray.

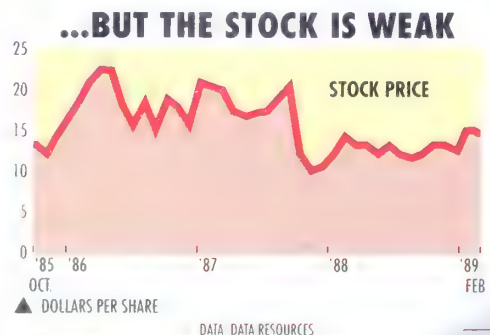
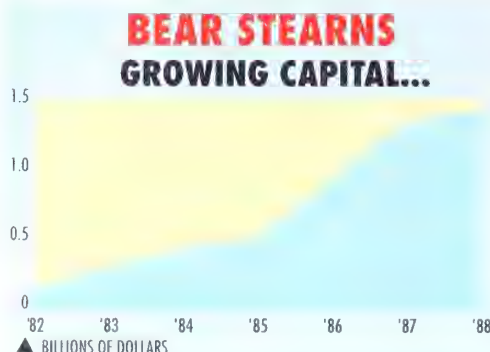
It is unclear whether it's in Greenberg's character to be an investment banker. Playing in the mergers-and-acquisitions game today requires long-term commitments of large sums of capital, anathema to any trader whose time frame stretches from one 10-second phone call to another. And Greenberg is a trader to his toes.

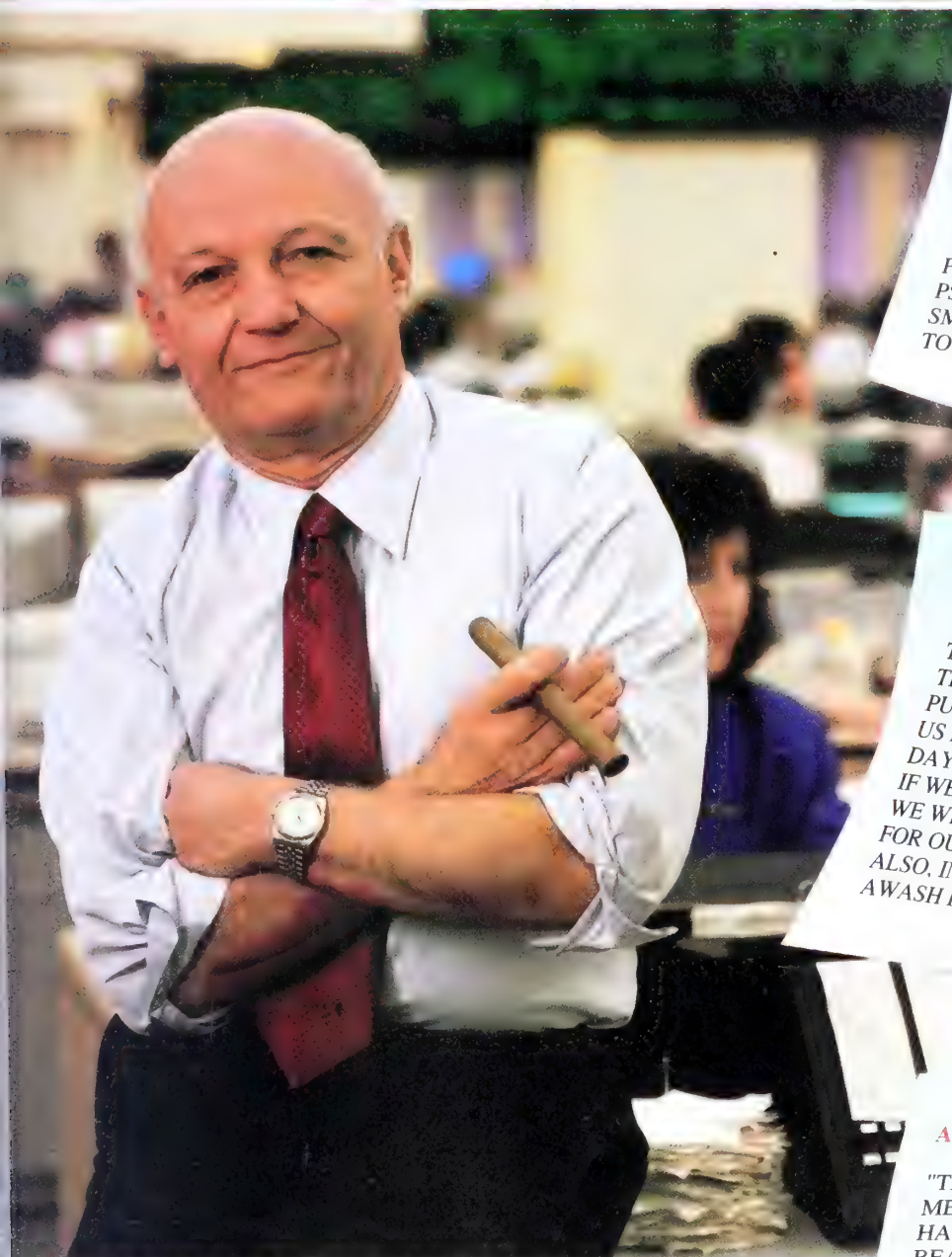
Even as his company pushes into investment banking, Greenberg remains uncomfortable with the concept. He still chokes on the term "merchant banking" and the notion of investing the firm's own capital as principal in leveraged buyouts. He once described it in a memo as "buying stock in a company whose shares are not publicly traded... in a business very different from what you are familiar with."

SHIRTSLEEVE BOSS. At first glance the Macanudo cigar-smoking, former college football player appears to personify the old gunslinger image. Greenberg is perhaps the best trader on Wall Street. He belongs to a small circle of raiders and money managers that have been turning Corporate America upside down. From his own chair on the trading desk, shirtsleeves rolled up, he bent into a phone, he buys and sells big blocks of stock for a special clientele—Ronald O. Perelman, Michael Belzberg, Irwin Jacobs, Consilium Partners, Charles E. Hurwitz, and other "financial entrepreneurs."

Donald Trump, the man who claims to have made dealmaking an art form, says: "He's got the best trading ability I've ever seen. He's made a lot of money with Aladdin, made money on Holiday Inn, Allegheny Federated, and Bally"—\$150 million by most accounts.

Greenberg didn't have the kind of social connections found at First Boston Corp. or Goldman, Sachs & Co. when he arrived on Wall Street.





MAY 5, 1981

"OUR FIRST DESIRE IS TO PROMOTE FROM WITHIN. IF SOMEBODY APPLIES FOR A JOB WITH AN MBA DEGREE, WE WILL CERTAINLY NOT HOLD IT AGAINST THEM, BUT WE ARE REALLY LOOKING FOR PEOPLE WITH PSD DEGREES. PSD STANDS FOR POOR, SMART, AND A DEEP DESIRE TO BECOME RICH."

AUGUST 9, 1985

"I HAVE JUST INFORMED THE PURCHASING DEPARTMENT THAT THEY SHOULD NO LONGER PURCHASE PAPER CLIPS. ALL OF US RECEIVE DOCUMENTS EVERY DAY WITH PAPER CLIPS ON THEM. IF WE SAVE THESE PAPER CLIPS, WE WILL NOT ONLY HAVE ENOUGH FOR OUR OWN USE, BUT WE WILL ALSO, IN A SHORT TIME, BE AWASH IN THE LITTLE CRITTERS."

AUGUST 15, 1985

"THE RESPONSE TO THE MEMO ON PAPER CLIPS HAS BEEN OVERWHELMING. BEAR STEARNS WILL NO LONGER PURCHASE RUBBER BANDS."

GREENBERG AND HIS STAFF MEMOS: GENEROUS IN PRIVATE, PENURIOUS AS CHAIRMAN

son of an owner of a chain of women's clothing stores in Oklahoma City, he led his first job as a clerk at Bear Stearns in 1949. New York's top investment houses weren't hiring many University of Missouri business graduates at that time. They still aren't. Then as Bear Stearns didn't care whether he went to an Ivy League school, Greenberg succeeded on performance, pedigree. A brilliant trader, at 25 he was running the arbitrage desk. At 29 he was trading at the elbow of Chairman "Cy" Lewis, the man who invented block trading. Two decades later he was sitting in Lewis's chair. To become a top investment bank on Wall Street, both Bear Stearns and its

chairman will have to alter their identities. This won't be the first time for Greenberg. At the University of Oklahoma on a football scholarship, before transferring to Missouri, he complained to his friend Alvin H. Einbender about trouble getting dates. Einbender, who is chief operating officer at Bear Stearns today, advised him to change his name, and he did—to "Ace" Gainsboro. The Gainsboro disappeared quickly but not the "Ace." Greenberg, 61, is divorced and remarried to a lawyer in her early forties. His son, Teddy, who used to write plays, now plays at risk arbitrage like his father. His daughter Lynn was the first woman to have a seat on the American Stock Exchange.

Greenberg is a strict disciplinarian when it comes to performance. He can be brusque, even ruthless. "When people are wrong, we feel they are not entitled to have any opinion. So if a guy has a loss, I'm not interested in his opinion any more. What do I care what he thinks? If it's down, I want out. Then we start over again. That's how we do it. There's no give on that."

Yet Greenberg's tough-guy demeanor is but one side of a far more complex

character. He took charge of Bear Stearns in 1978, the same year that John H. Gutfreund assumed control at Salomon. Greenberg turned a small, old-line partnership that did institutional trading and arbitrage into a broad-based public company that is one of the top three or four houses in equity clearing, mortgage-backed securities, program trading, risk arbitrage, and retail brokerage to high-net-worth (i.e., rich) individuals.

Bear Stearns had \$46 million in total capital the year Greenberg became chief executive officer. When he took Bear Stearns public in 1985, it had \$517 million. Today, it has \$1.4 billion. What's more, he did it his way—by keeping Bear Stearns independent during an era that saw such blue-chips as Lehman Brothers, Dean Witter, PaineWebber, E. F. Hutton, and Shearson gobbled up.

Like many who have made it big, Greenberg is an uncommonly generous private person—but he is fanatically penny-pinching as chairman of the board. Last fall he stood at a podium in front of 1,000 people at a United Jewish Appeal annual dinner and gave away \$1.1 million. Two weeks later, Greenberg chaired the New York Police & Fire Widows' and Children's Benefit Fund. He insists that Bear Stearns managing directors give at least 4% of their compensation to charity.

PENNY-PINCHER. Greenberg's frugality is legendary on Wall Street. In biting memos, he constantly admonishes the troops to save pennies. This frugality translates into the tightest cost control of any investment house on Wall Street.

Merrill Lynch & Co. may have the most customers, and Salomon may still be the biggest bond trader, but Bear Stearns has long been far more profitable than either. For most of the 1980s, Bear Stearns' 25% return on equity has been twice the industry average. Last year it's ROE was three times that of Shearson Lehman Hutton Inc. Only Morgan Stanley & Co. has been able to beat it—and just barely.

Since the firm went public in 1985, it has moved into the juiciest business on Wall Street:

FEBRUARY 3, 1988

"IT WAS JUST ANNOUNCED THAT SOME PROMINENT PEOPLE IN M&A JUST LEFT A FIRM BECAUSE OF A DIFFERENCE OF OPINION OVER STRATEGIC PLANNING. AN ISSUE LIKE THAT COULD NEVER ARISE AT BEAR STEARNS BECAUSE WE HAVE NO STRATEGIC PLANNING."

investment banking, including mergers and acquisitions; financial advice, and merchant banking. The firm traditionally serviced midsize companies, but now "we are going after major investment-grade clients," says Alan D. Schwartz, head of corporate finance. "We're committed to making Bear Stearns one of the top five investment firms."

Contrary to his gunslinger image, Greenberg runs a conservative shop that resembles an old-fashioned bank more than a brokerage. The firm generates most of its revenues from businesses that are as risk-free as possible. Interest income from lending money

amounts to 35% to 50% of revenue.

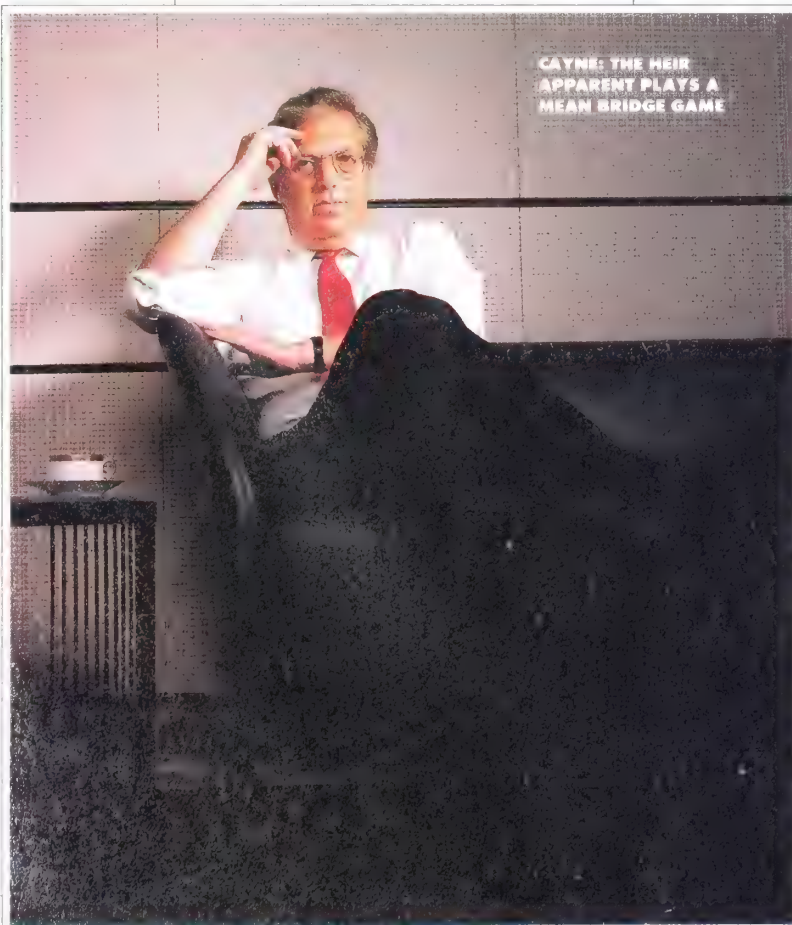
Back in 1973, when Bear Stearns moved its headquarters to 55 Wall St., it tripled its space. But the stock market was ailing. "God, we had empty rooms," says Greenberg. "We went to some brokers and said we'd give them free rent if they'd clear with us." Gerald Tsai was one of the first customers to settle trades through the Bear Stearns. He is still a client. Robert N. Gordon, president of Twenty-First Securities Corp., says that "in 1983, I was starting out. Pershing was cheaper but Bear Stearns knew a lot more about clearing. They're the smartest, not necessarily the cheapest."

LOTS OF 'FLOAT.' Clearing is a very smart business to be in. In the process of matching stock trades, Bear Stearns finds itself with \$3 billion to \$6 billion in free credit balances at any point in time. This "float" is similar to the float that American Express Co. gets on travelers' checks. It's the float—the use of money from the time the firm collects funds until the time that it must pay them out—that makes clearing a low-risk business. The firm uses the money to help finance its own activities, thus cutting its borrowing costs.

Bear Stearns also skims the cream of the retail brokerage market. The profit of the average customer? "He's a substantial investor, a high net-worth investor," says James E. Cayne, president of the company, who runs the sales force of 700 brokers with big regional offices in Chicago, Los Angeles, San Francisco, Boston, Dallas, and Atlanta. "Some of our retail clients look like institutions."

Bear Stearns earns big commissions from these rich clients. Some firms charge as little as 5¢ a share to trade big blocks. At Bear Stearns, the lowest commission cost is 7¢. But the real gravy is in margin. Brokers lend to clients who play the market with borrowed money.

When a client signs a margin agreement, it allows the firm to borrow his shares. The brokerage takes the stock and lends it to clients who want to sell short. The short-seller usually borrows



50% of his own money on the line and is charged interest on the rest. The firm, however, receives the entire amount of the fee from the buyer. So margin accounts are, in effect, money in the bank to a brokerage firm. Nearly 300,000 individuals and institutions have accounts with Bear Stearns. Most of them are margin accounts.

The firm also arranges margin loans for smaller clearing firms, which in turn lend to their own clients. The company borrows from banks and then lends money as margin to clearing customers. The interest-rate spread between the two is pure profit. It's a business that Bear Stearns codifies. "We treat these accounts as family," says Cayne, Greenberg's heir apparent.

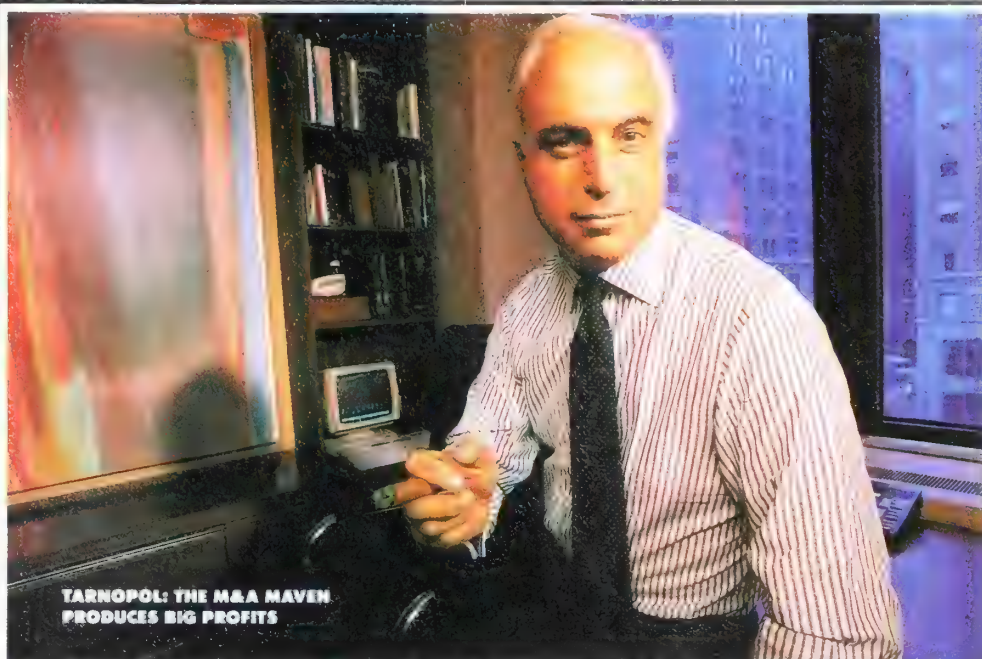
Michael L. "Mickey" Tarnopol, head of M&A, knows just how hard it will be to change Bear Stearns into a firm that makes most of its money from big trading customers to an investment banking house. Tarnopol left Goldman Brothers in 1975 to join Bear Stearns following a vicious battle between the investment bankers, led by Herman Pete Petersen and the upstart firm, led by Lew Gluckman.

Tarnopol took charge of M&A in 1985 when the decision was made to move into the market. He immediately began lobbying for more capital. "It wasn't easy. The culture was to maintain liquidity."

BIGGER SLICE. As the total capital of the firm increased over the years, the investment-banking side got a bigger slice, but it was never enough. What has really made the success—and the huge profits—possible is success can bring. Bear Stearns was a principal in the LBO of Cole-Haan shoes in 1986. It invested \$18 million. It sold the company to Nike Inc. for \$96 million 22 months later.

That kind of profit is hard to ignore. The managing directors are smart enough to see where the money is being made—in the investment-banking business," says Tarnopol. "Our job is a hell of a lot easier today convincing Bear Stearns to make an equity investment or commitment on a longer-term basis than it was last year and the year before." Since 1985, revenues from investment banking have increased from 9% of total to 18%.

The big money is in investing your firm's capital, and the investment-banking side wants to deal in size. Their eyes are on Bear Stearns' liquid balance sheet which could easily support more long-term commitments. The balance sheet is a very valuable tool," says Tarnopol. "One of the things we look forward to,



quite frankly, is to tap into that balance sheet as we go along."

Others don't see it quite that way. "We don't want to rent our balance sheet in order to do business," says John C. Sites, head of the mortgage department. "We have very, very few principal investments. We have no bridge loans on the books at all. It's too risky. My children's trusts are in that balance sheet."

But without big capital commitments, Bear Stearns will have a hard time making any serious headway in investment banking because everyone else is putting up their own money for deals. And unlike First Boston, Morgan Stanley, or even Salomon Brothers, the Bear doesn't have a name that opens corner-office doors. It doesn't have the junk-bond clout of Drexel either. "All we ever ask for is a chance to compete," says Schwartz. "What's difficult for us to live with is closed doors."

So far, the firm has been able to piggyback on Greenberg's old trading contacts with financial entrepreneurs. It put together a big savings-and-loan deal late last year for Ronald Perelman, and it has financed several Trump casinos.

APRIL 15, 1988

"EFFECTIVE TODAY WE HAVE A NEW POLICY. NOTHING GOES OUT OF BEAR STEARNS WITHOUT THE SENDER'S IDENTIFYING MARK IN THE UPPER LEFT HAND CORNER OF THE ENVELOPE. THIS WILL SAVE US TIME, MONEY, AND AGGRAVATION. IF YOU ARE TOO BUSY TO DO THIS, PLEASE CALL ME. I WILL BE GLAD TO COME DOWN AND PUT THE PROPER IDENTIFICATION ON YOUR MAIL."

Bear Stearns has also been able to offer creative financings and swaps in yen, swiss francs, and other currencies to save money for such blue-chip corporations as Ford Motor, Monsanto, and Walt Disney. It hopes that they will lead to long-term relationships.

The strong high-end retail operation is another source of leads for investment banking. Bear Stearns did one of the first big LBOs back in 1983 for John W. Kluge when he took Metromedia Inc. private. Kluge had a strong personal relationship with Mike Oppenheimer, a broker at the firm.

But Bear Stearns has a special problem. Trust is vital to establishing quality, long-term ties between top-rated corporations and investment banks. Bear Stearns' reputation as a ruthlessly aggressive New York organization doesn't help much. Clients talk to one another, and the word is out: Beware the Bear. In a recent private placement for Triton Group Ltd., Bear Stearns hiked its fee from 2 to 3.5 percentage points after Triton had committed itself to the buyout. Triton was furious.

'PILLAGE AND PLUNDER.' Bear Stearns has also angered some because of its poor trading manners. "When they knew the customer was ignorant, they took advantage of it. All firms do that, but Bear Stearns did rape, pillage, and plunder," says one woman who has worked on the trading desks of First Boston, Salomon, and Bear Stearns. Greenberg calls that "100% wrong."

Worst of all, it has a reputation for skirting close to the edge of legality. In 1986, Bear Stearns invented an option agreement that only raiders could love. Investors buying \$15 million or more of a company's stock must notify the Federal Trade

Commission and the Justice Dept. If they buy stock and hide it, they are guilty of "parking." Under the option agreement, Bear Stearns buys stock in its own name and sells the client an option to buy. The client agrees to pay Bear Stearns for any losses. In effect, the option agreement allows raiders to control stock in a company without actually owning it. This kind of agreement was used in nearly 25 raids, including Donald Trump's effort to take over Bally, Wickes Cos.' run at Owens-Corning, and the Belzbergs' push against Ashland Oil. Justice's Antitrust Div. filed suits against Wickes, Trump, and the Belzbergs. The SEC sued the Belzbergs separately. All settled with Justice. Says Greenberg: "The FTC knew what was going on for years. It was no secret. Our clients' lawyers approved it. The FTC decided they no longer thought it was good. Trump, the Belzbergs, and Wickes got slammed. Then we stopped it."

CARD PLAYERS. High-stakes bridge is a passion for Greenberg. Nearly every day after the close of trading he plays at the private Regency Whist Club on Manhattan's East Side. Laurance A. Tisch and Milton Petrie are also among the regulars. People have been known to drop a few thousand dollars in one rubber. Greenberg and Cayne are among the top 100 bridge players in the country. In describing his game, Greenberg reveals a more general philosophy: "Everybody in business is a gambler. Somebody in the dress business who brings out a line three times a year is taking a gamble. Every businessman takes calculated risks. Good businessmen take good calculated risks. Bad businessmen take dumb ones. Bridge is like that—calculated risk."

Only a few Wall Street firms have made the transition from a great trading house to an even greater investment bank. There are major disputes over how capital should be used, short-term or long-term. There are fights between the trading and investment groups. Bear Stearns is no exception. Its trading culture leads everyone to be his own profit center. There is little emphasis on teamwork—crucial to investment banking.

In the end, the major problem may be Alan Greenberg himself. His first love is trading, and his talent is in accumulation, amassing blocks of stock better than anybody else on the Street. A bridge hand is played in a short span of time. So is a trade. Building a team may not be that important to him right now. It's a change of identity he may not be willing to make. In the end the gunslinger may be a loner.

By Bruce Nussbaum in New York, with bureau reports

NOW THE INFLATION BATTLE IS INSIDE THE FED

It's Beltway doves against the hawkish Out-of-Towners



SAN FRANCISCO'S PARRY: FAR OUT OF STEP WITH WASHINGTON SUPPLY SIDERS

When a senior Federal Reserve official warns that "Things are really hot right now," he's not talking about the tiff between Fed Chairman Alan Greenspan and President Bush. Conflicts between a growth-oriented White House and an inflation-fighting Fed are old hat. What worries Fed insiders is the rift between the Beltway Gang and the Out-of-Towners—the Washington-based Board of Governors and the 12 regional Fed banks.

For almost a year, regional chiefs have pushed for a tougher stance on inflation than most Washington governors could stomach. With January's price surge, both camps agreed that higher interest rates were needed to slow the economy. But the conflict isn't over. In coming weeks, the robust growth and price statistics expected for February will reignite the dispute. While the governors tend to see this winter surge as inflation's last hurrah, the Out-of-Towners are likely to press for still-higher rates. Over the longer term, the fight for influence between the regions and headquarters will determine whether the Fed fights one battle at a time

or tries to vanquish it permanently.

When the board raised the discount rate from 6.5% to 7% on Feb. 24, Washington seemed to be extending an olive branch. All 12 regional presidents asked the Board to raise the rate, a symbol of the Fed's inflation-fighting resolve. Most of them took the same line in recent secret Fed policy meetings. The Board's discount-rate move was enough to please everyone: The Cleveland Fed had asked privately for a 100-point increase. But for a while, everyone was singing the same tune.

SPEED LIMIT. The harmony didn't last long. Four days later, Vice-Chairman Manuel H. Johnson spoke on the floor, trying to control inflation by setting growth at some ideal rate. Buried in the jargon was a clear message: The supply-side governors, like Martha R. Stewart and Johnson himself, won't let their regional Feds' inflation fears impose an arbitrary "speed limit" on the economy.

Until recently, a serious bid for peace by the regional presidents would have been almost inconceivable. "Five years ago, nobody gave a damn who the regional presidents were," says one ex-

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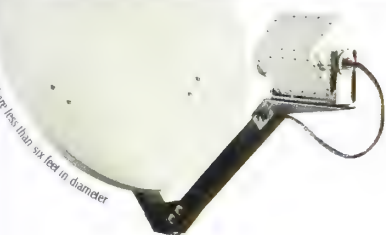
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watcher. Other than the New York Fed chief, who runs the Fed's domestic and international market operations, the presidents have always been the poor relations of monetary policy.

New York Fed President E. Gerald Corrigan, a protégé of former Fed Chairman Paul A. Volcker, is still the undisputed No. 1. But other Out-of-Towners are making their mark. As the dean of Fed presidents, Richmond's Robert P. Black is respected for both his economic analyses and his 15 years' tenure. Several Fed officials mention Edward G. Boehne, an eight-year veteran at the Philadelphia Fed, for his consensus-building skills.

When it comes to taking a hard line, though, relative newcomers stand out. Thomas C. Melzer seasons the St. Louis Fed's traditional focus on the money supply with his 17 years at Morgan Stanley & Co. When Melzer speaks, says a former staffer, "people listen. He's not an academic or a forecaster—he made his living trading bonds."

San Francisco's Robert T. Parry warns that growth above the long-run trend rate, the 2.5% or so a year that comes from labor force and productivity increases, "cannot be sustained in the long run without inflation." That puts Parry, former chief economist at Security Pacific National Bank, far out of step with the supply-side governors Ronald Reagan put on the Fed board.

'POWER VACUUM.' Cleveland's Lee Hoskins rejects any theoretical trade-off between growth and inflation, but he's still an inflation hawk. The former chief economist of Pittsburgh's PNC Financial Corp. wants the Fed to declare a goal of zero inflation within five years. The public, he says, "recognizes

neither costless nor an acceptable solution to our other economic problems."

More important than what they say in public, the presidents' arguments within the Fed can carry the day on policy. "Today's presidents are the most articulate, most analytic group in modern history," says ex-Governor Lyle E. Gramley, who sees "a bit of a power vacuum at the top."

But intellectual firepower alone wouldn't



CLEVELAND'S HOSKINS: AIMING FOR ZERO INFLATION

have gotten the presidents very far. Their status began to change when Volcker found himself increasingly challenged by Reaganite governors who disliked his inflation-fighting fervor and his heavy domination of policy. As the chairman reached out to the presidents for support, recalls one regional staffer, "the attitude changed from, 'Are you a governor or a president?' to, 'Are you in the inner circle or out of it?'"

Greenspan's 1987 appointment ended Volcker's close-to-the-vest style and spread the power around. As a business forecaster, Greenspan had long-standing relationships with most of the presi-

dents, including former clients Hoskins and Parry. The regionals' close ties to local bankers and executives makes them, as a staffer says, "the CIA of domestic economic intelligence"—and endears them to information junkie Greenspan.

While Fed officials admit the split exists, they say the divisions aren't clear-cut. The presidents take a harder line on inflation than the Beltway crowd, but doves can be found in the banks as well as at the Board. All Fed supply siders are in Washington and all monetarists are out of town—but few Fed officials adhere to either ideology. "There isn't any bloc voting, presidents vs. governors," says a board member.

Still, the distinctions are real. In a Fed culture that values experience, presidents have more tenure. They average 6½ years, vs. 2½ for the governors. Eight of the 12 senior Fed officials during the harrowing 1979-82 inflation fight, an ordeal that not one of the governors witnessed from inside. Says one Fed-watcher: "If you're looking for the traditional central bankers these days, don't look in Washington."

SHIFTING DEBATE. For the short term the dispute tends to be a bit arcane. While Governors Johnson and Wayne Angell champion supply-side analysis of commodity prices as a barometer of inflation fears, the presidents prefer to view such direct measures as growth, wages, employment, and consumer prices. Throughout 1988, the clash between hawks and doves mainly affected timing. "If everyone had agreed with the hawks, rates might be a half-point higher—not much in a year when we

raised rates 2½ points," says a regional staffer.

But over the long run, the debate shifts to defining a tolerable level of inflation. As the economy slows, the Fed must sustain growth while continuing to squeeze inflation. "None of us wants a recession," says a hawkish president. But to want the Fed's hard-won gains against inflation to slip away, either. Whether he can balance those conflicting goals will determine Greenspan's place in the pantheon of Fed chairmen.



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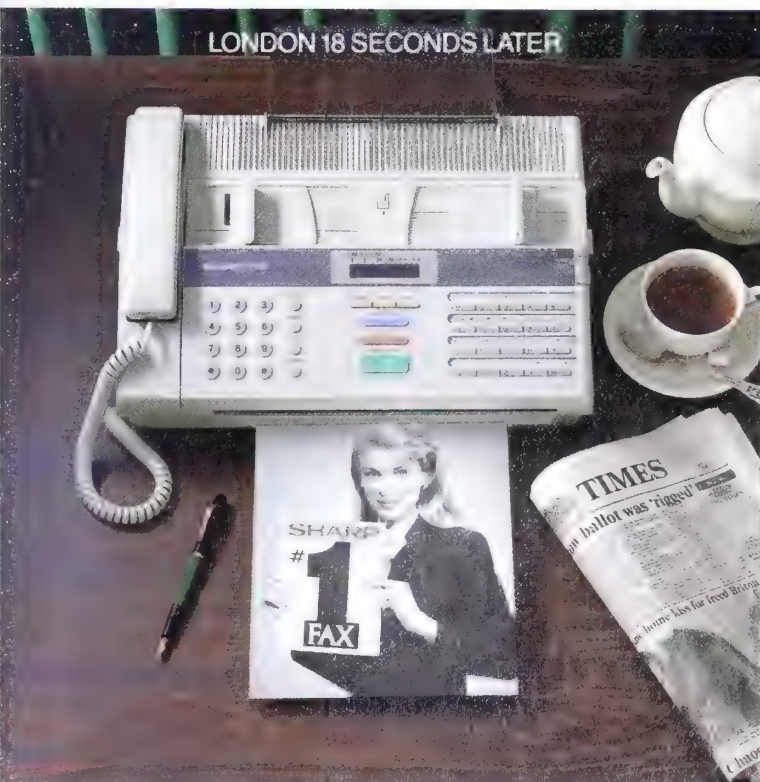
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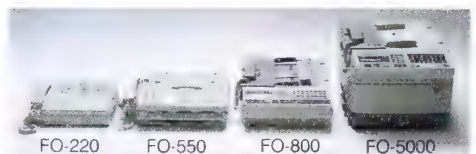
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THE FINAL FRENZY OF A PENNY STOCK SHOP

Justice is investigating now-defunct Investors Center

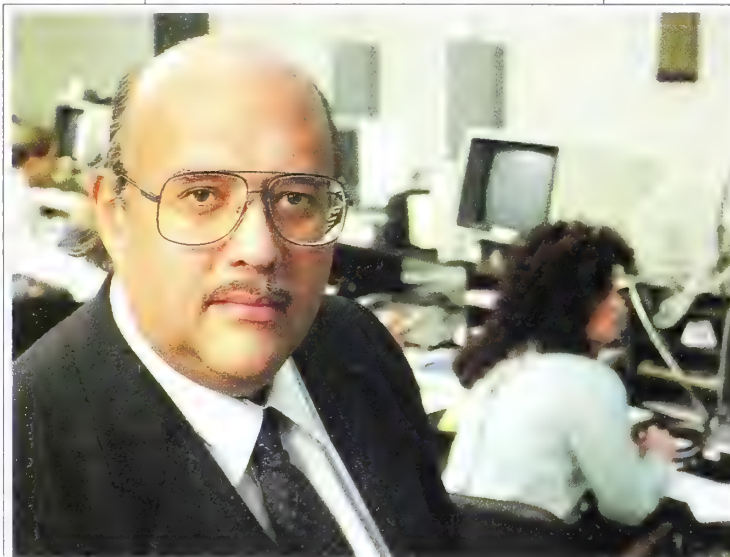
From the start, Investors Center Inc. was a frenetic place. Although a scant five years old, it rapidly built its stable of aggressive young brokers to about 900. That's more than many a venerable and diversified Wall Street house, yet IC concentrated on about 15 issues—penny stocks pitched to individuals who, somehow, had a lot of trouble cashing in on the gains that they kept hearing about.

The pace got even more frantic at the end. As IC closed its headquarters in Hauppauge, N. Y., on Feb. 23, the principals hired bouncers to protect themselves from distraught salesmen. Police were called as some brokers made off with computers and threw chairs out the window. Two senior executives ended up at a police station—each charging the other with stealing his client books.

The collapse was destined to come and to be messy. About half of IC's \$12.6 million in assets was tied up in stocks it promoted—and propped up as long as it could. After *BUSINESS WEEK* published its investigation of IC (BW—Jan. 23), its brokers started to cash their clients out of the firm's stocks. Their prices evaporated, along with IC's net worth and the once-dazzling paper gains of thousands. **'AGGRESSIVE STANCE.'** The National Association of Securities Dealers, the industry's over-the-counter cop, began putting on the heat in December. The NASD said the firm could no longer hold customers' cash or securities, requiring instead that it clear all transactions through an outside firm. IC Chairman Anthony J. Stoisch has acknowledged that the Securities & Exchange Commission has subpoenaed records.

But perhaps most ominous for the penny stock clan, the Justice Dept., which can bring criminal charges, is joining the fray. When a Justice official refused to comment on IC, several former IC brokers say they have been contacted

by the Federal Bureau of Investigation. The Justice official did, however, say that "obviously there is some sense that civil remedies are insufficient. Our office is prepared to take an aggressive stance" toward penny stock abuses. Other sources say that could include charges under the Racketeer Influenced & Corrupt Organizations Act (RICO), which lets prosecutors freeze some of



■ **TONY STOISICH: ONLY DAYS AFTER IC SHUT ITS DOORS, HE'S HELPING SET UP NEW PENNY STOCK OUTFITS**

the assets of defendants before a trial.

Stoisch didn't return calls. His attorney, Ira L. Sorkin, says the SEC's subpoenas don't necessarily indicate that IC itself is being investigated, adding that Stoisch closed the firm "with the principal goal of protecting customers."

Investigators are said to be focusing on whether IC "dominated and controlled" markets for its stocks and manipulated their prices to the detriment of its customers. IC often quoted its issues hundreds and even thousands of percentage points above their offering price. "Before I told them that I wanted to sell, they told me: 'You've got a great

investment, the stocks are way up,'" says Daniel V. Andreozzi, an investor in Houston. But, he adds, he never could get the firm to sell his shares.

And outside of a tight circle at the top, even IC brokers couldn't always get in on the firm's hot new issues. According to former brokers, the stock of Eagle Pharmaceuticals Inc., which soared a reported 2,800% in 1988, is just such an example. Angelo D. Crisci, a senior IC executive, brought Eagle public at a penny, says a former branch manager, "but the brokers couldn't touch it until it hit 12¢. He just sat there" with stock for his favored customers and top IC executives. Records for Eagle have been subpoenaed by the SEC; Crisci couldn't be reached for comment.

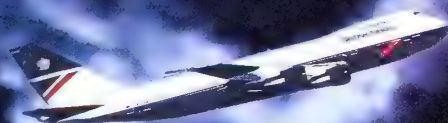
BIGGEST MONTH. Then there's the case of All-Quotes Inc., one of the last firms IC brought public. The prospectus lists Pamela Schmuch as an All-Quotes insider. She handed out awards at IC meetings and is described by several ex-brokers as IC head trader Joseph J. Diangelo's girlfriend. Public investors in All-Quotes paid 4¢ per share. Cheap enough, it would seem, except that they were paying 40 times more than Schmuch and other insiders. Diangelo and Schmuch couldn't be reached for comment.

Despite the cloud it was under by January, former brokers said that was one of IC's biggest months for commissions. Unfortunately for most IC brokers they say that either they

weren't paid for January or the checks bounced. The checks to customers were bouncing, too, and the SEC on Mar. 1 asked to have Securities Investor Protection Corp., a government-chartered private fund, step in to handle the liquidation. SIPC would make good on any cash balances held by IC and send clients their stocks—worthless or not.

Undaunted by IC's fate, Stoisch is already helping IC personnel set up other penny stock firms. Among them are M.J. Sterling in Great Neck, N.Y., which is registered in the name of Michele Fay Grunfeld, the wife of a former IC branch manager. Stoisch is also helping his former head traders, Diangelo and Craig O. Roer, form a firm, as yet unnamed. Old penny stock firms may fade away, but not faster than new ones can fade in—as long as investors can be lulled by the hope of scoring big on tiny stocks.

By David Zigas in New York



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BY GENE G. MARCIAL

A BELEAGUERED BOEING MAY BE ON LOCKHEED'S TAIL

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So what has been firing up Lockheed's stock recently? The takeover talk among some pros is getting louder. And they believe the buyer could be Boeing. Since it, too, is a major defense contractor, Boeing would have no problem getting Pentagon approval. And perhaps because of the problems this major commercial jet-aircraft maker is having (page 34), Boeing "wants to increase the military end of its business to about 45%—by acquiring Lockheed," says one influential money manager who has been buying shares. Neither Lockheed nor Boeing will comment on anything having to do with takeover speculation. Boeing can well afford to buy Lockheed, this investment pro believes. The company has about \$4.2 billion in cash, with little debt, he notes.

"Lockheed is extremely undervalued, trading at less than half its breakup value," says David Loomis, an analyst at 13D Research. He notes that, at 48, the stock sells for only 7.4 times estimated 1989 earnings. Based on recent takeovers in the industry, he says, Lockheed is worth \$100 a share. Assets include 320 acres of high-priced real estate in Burbank, Calif.

ROCKETING PROJECTS. Boeing's government business, which accounts for 32% of revenues, hasn't been a big profit booster. Military sales, which totaled \$5.5 billion last year, are expected to be relatively flat in 1989, says one analyst. In contrast, Lockheed's military projects have grown more than 30% a year since 1982. The classified military projects account for almost 50% of operations, says Loomis.

Large-block buying of Lockheed shares has been noticeable of late. One trader says Salomon Brothers has been aggressive and is thought to be buying for a client. And Texas financier Harold Simmons, through his 88%-owned Valhi Inc., sought clearance from the

LOCKHEED IS FLYING HIGH



Federal Trade Commission to buy up to 15% of the company. Valhi has acquired 375,000 shares, or 0.63%, for \$15 million.

But Simmons insists he doesn't intend to make a bid. Apart from being a nondefense company, Valhi is small compared with Lockheed. And the financial firm has revenues of \$2.2 billion vs. Lockheed's \$10 billion. Nevertheless, says Loomis, the Simmons move will prompt Lockheed to accelerate a restructuring, possibly by selling assets, repurchasing shares, and sharply raising the dividend.

SINGING ALONG WITH SPEC'S MUSIC

When insiders unload a big piece of their company's stock, the share price usually falls. Not at Spec's Music. The largest retailer of records and video products in Florida was 60% controlled by the Spector family. When they dumped some 500,000 shares in mid-February, the stock shot up from 6½ to nearly 8.

The sale of the big block added liquidity to the stock by increasing the float, or the number of shares in public hands, from 1.8 million to 2.2 million. And that bigger float enabled institutions to buy in, says Chairman Martin Spector. Analysts were impressed by the eagerness of some big investors, including Gintel Equity Management, Wellington Management Fund, and OTC Securities Fund, to snap up the Spector family's shares.

"The company, with its 43 stores, is a standout in its business and sports a strong balance sheet, with good pros-

pects of growing about 20% a year," says one of the investment managers who bought in. He notes that Spec's revenues are in an upswing, climbing from \$26.5 million in fiscal 1987 to \$32.5 million in 1988. They are projected to hit \$40.9 million this year and \$52.5 million in 1990. Earnings jumped from 32¢ a share in fiscal 1987 to 46¢ last year, with 65¢ expected for 1989 and 75¢ seen for 1990. With these numbers, this money manager thinks the stock will double in the next year or so.

Spec President Ann Spector Lieff says the company is aiming for sale of about \$100 million by 1993. Spector Lieff, her father, Martin, and a sister still own about 49% of the company.

IS SHEARSON NO. 1 ON AMEX' SELL LIST?

Expectations are rising among analysts and big investors that American Express Chairman James Robinson may try to wake up the company's sleepy stock. Shares of the travel and financial-services company, now at 29, have been lagging behind the market for years.

Some pros say Robinson might announce a large share repurchase at a meeting with analysts scheduled for Mar. 9. To finance some of the buyback, they say Robinson will sell part of not all of American Express' remaining 62% stake in Shearson Lehman Hutton.

"There is growing pressure on management" to get better value for the company's profitable financial-services businesses, notes Arthur Kirsch, director of research at Drexel Burnham Lambert. Robinson is said to be waiting for another market rally to get a better price for Shearson's depressed stock. "But he might decide not to wait any longer," says a California investment manager who has a big stake.

Robinson certainly wants to diversify the problem businesses that American Express has acquired over the years. "The Street is getting impatient with American Express' ongoing earnings problems, particularly at Shearson," says Kirsch. He notes that Shearson diminishes the value of American Express' stock because the market assigns a low earnings multiple to stock brokers. Frank DeSantis Jr., an analyst at Smith Barney, expects the company to eventually retain or sell Travel Related Services and IDS Financial Services. A spokesman declined comment on the analysts' speculation.

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COMPAQ VS. IBM: PEACE COMES TO SHOVE

Their rivalry in PCs has become 'a titanic power struggle'

Compaq Computer Corp. has been like a fly on IBM's back—annoying but not a big problem. Even after Compaq became Big Blue's strongest rival in office PCs, IBM practiced peaceful coexistence. But that has changed. Last fall, Compaq vowed that it and a group of other PC makers would displace IBM in setting "industry standards" for PC hardware. Now, IBM is swatting back, starting what David A. Carnevale, an analyst for market researcher InfoCorp., calls a "titanic power struggle over the future of the industry."

That became clear on Feb. 20, when President Rod Canion ended a seven-year relationship with Businessland, the computer chain that accounts for 7% of Compaq's revenues and is a key link to corporate customers.

Canion took his gamble after IBM began selling PCs to Businessland and ComputerLand, the two largest chains, at 44% off list—four points better than other dealers get from IBM or Compaq. The extra money boosts commissions and advertising for IBM gear.

Suddenly, Businessland Inc. Chairman David A. Norman publicly sided with IBM. He also demanded that Compaq, which produced 15% of Businessland's sales, match IBM's discount. Instead, Canion pulled out. "We're not going to hurt other dealers to help one," says Michael S. Swavely, Compaq's vice-president for sales. "IBM is just trying to reverse its decline."

Indeed, nearly two years after introducing its PS/2 computers, IBM is still trying to make its chief innovation, the microchannel, the industry standard. IBM "has never been more aggressive," says ComputerLand Corp. Chairman William Y. Tauscher. It has wooed retailers by eliminating unpopular sales quotas and hiking allowances for training and support. IBM reps even make joint sales calls with dealers.

None of this has hurt Compaq much. In late 1986 it beat IBM with the first

IBM-compatible PC to use Intel Corp.'s powerful 80386 microchip. Slow IBM product introductions and confusion over the microchannel—a method for attaching printed circuit cards—made Compaq the leader in the 80386 business, which produces half its sales. It won 56% of

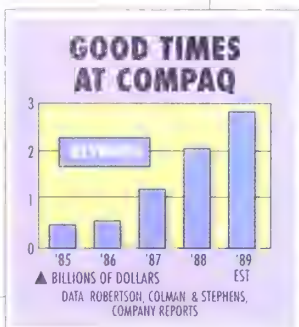


CANION: HIS SPLIT FROM BUSINESSLAND MAY BE A SAVVY MOVE

that market vs. IBM's 33%. These speedy desktops are in hot demand because they can do the same work as more expensive minicomputers.

Compaq's revenues more than tripled, to \$2.1 billion, since 1986, and earnings rose sixfold, to \$249 million. Meanwhile,

IBM's share of the U.S. PC shipments fell from 39% in 1986 to 32.6% last year, says market researcher StoreBoard Inc. And Microchannel machines are only 9% of all PC sales, estimates InfoCorp. That slow start gave Compaq an opening last fall to propose an alternate design called EISA—extended industry standard architecture.



Backed by eight other suppliers, EISA intended to mimic—and displace—proprietary microchannel.

That challenge roused IBM. On the Compaq split with Businessland, it was extolling the microchannel for securities analysts in Boca Raton, Fla. "They're trying to make sure EISA is stillborn," says Aaron Goldberg, analyst at International Data Corp. Compaq Chairman Benjamin M. Rosen says it won't work: "This battle isn't going to be won by public relations."

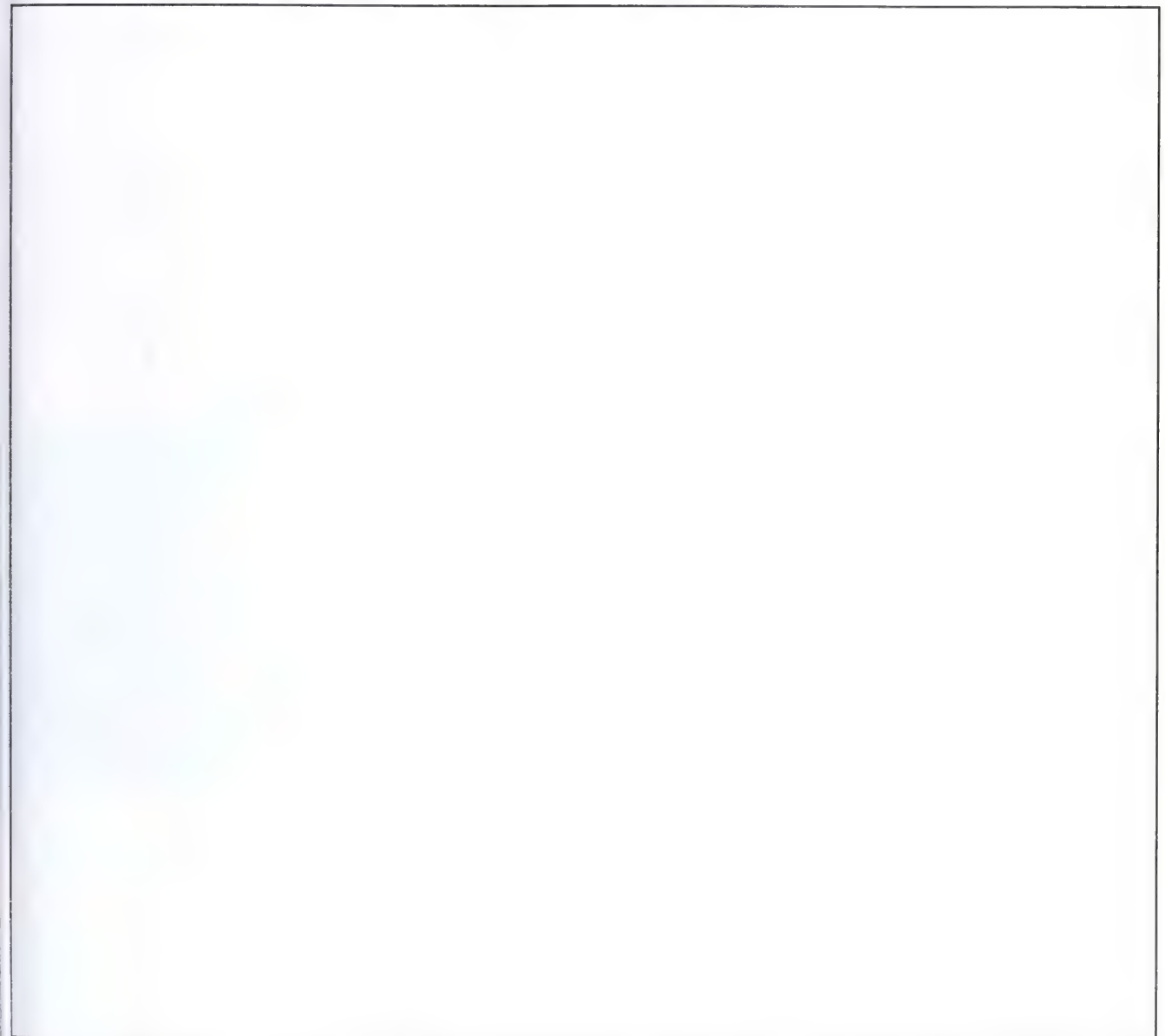
Maybe not, but IBM is rebounding. Its share of PC sales through retail stores rose to 35%, says StoreBoard. A new PS/2 without the microchannel helped. So did price cuts of 10% to 15%. In February, Compaq cut prices, too. And analyst James Weill of Soundview Financial Group sees more ahead. "Margins will drop," he says. That bad news for Compaq is partly reflecting the costs of rapid expansion, its gross margins have already fallen 40%—from 45% in 1986.

'SETBACK.' Compaq is undaunted. Thanks to its strength in 80386 systems, a market that may double this year, Swavely says "we could lose half our market share and still see sales there grow 50%." The company also plans new products this year, including the fast 80386 system yet another 80386-based laptop. But Compaq's EISA computers, expected in 1989 will be the test. If EISA fails, it'll be a major setback," says Weill.

If past performance is any guide, Compaq probably will pull it off. Canion's break with Businessland seemed uncharacteristically emotional reaction. But some observers now see the move in this move. By publicizing Businessland's IBM discount, Compaq may force other dealers to demand the same discount from Big Blue. If IBM gives in, its profits may suffer. If it holds fast, consultant Seymour Merrin of Merrin Information Services in Palo Alto, Calif., the less-favored dealers may be inspired "to go out and sell Compaq." That could make Compaq the surprise winner of this skirmish at least.

By Mark Ivey in Houston and Geoffrey in New York, with bureau reports

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DEALMAKERS ARE BURNING UP THE PHONE LINES

From the U.S. to Europe to Asia, the business has gone merger-happy

It was one of those gray December days when New York's Times Square looks particularly down on its luck. But inside the nearby Marriott Marquis hotel, John F. Akers was grinning like a blackjack player whose last draw just made 21.

IBM's chairman was telling reporters about a huge deal to sell his bleeding ROLM phone equipment business to West Germany's Siemens. This didn't mean IBM was licked in telecommunications, said Akers, eyes twinkling. Big Blue would profit more from having Siemens share the load of selling communications gear. Before long, his playful delivery had Siemens' normally reserved chairman, Karlheinz Kaske, chuckling at the irony of the event, while other IBM and Siemens executives ex-

changed nervous glances and tittered. Two of the world's biggest high-tech adversaries, IBM and Siemens had been butting heads for years. And now they were bosom buddies.

If that seems amazing, consider this: Not in 100 years has the staid, \$500 billion telecommunications business seen such deal mania. From the U.S. to Europe to the Far East, companies are joining forces, buying into fledgling businesses, or hitching a ride on one another's hot strategy. The idea is to limit the risk in attacking new markets by spreading the investment load or buying a rival that does it better. Much of this takes the form of joint ventures. But in 1988 phone companies also spent \$4.5 billion on mergers and acquisitions,

eight times the figure in 1987. And the pace is likely to quicken. Says Jack Grubman, telecommunications analyst at PaineWebber Inc.: "There are going to be a lot of big checks written in the next couple of years."

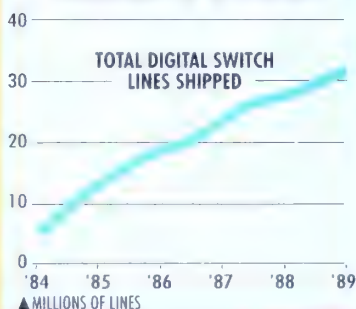
Various forces are driving this zeal for deal. In the \$106 billion phone equipment business, single-digit revenue growth and falling prices are forcing consolidation as the market leaders buy weaker companies to keep expanding. In just the past six months, American Telephone and Telegraph Co. has agreed to gradually take over GTE Corp.'s sagging central office switch business by 1995. AT&T also bought Paradyne Corp., a troubled maker of computer communications equipment. And it just outgunned international rivals for a deal that will give it

A SQUEEZE ON EQUIPMENT MAKERS...

R&D COSTS KEEP RISING...



...AS GROWTH IN DEMAND IS SLOWING...



...AND PRICES ARE FALLING



DATA: DATAPRO/NBI

ent chunk of the \$28 billion that Italy ns to spend on its network in the next r years. AT&T and state equipment ker Italtel will jointly develop and ke switching and transmission equip- nt for rebuilding the country's rickety one network. And AT&T will help Ital- market its products internationally. n the \$400 billion business of moving ls and data—the phone service busi- s—the motivation to deal is mostly ensive. "Technology is allowing you come up with new ways to do v services and products," says Sam L. n, chairman of Pacific Telesis Group San Francisco. "And it's driving vn costs, which drives up demand— l opportunity."

TECHNICAL EDGE. Thanks to improve- ments in radio transmission and plum- ing equipment prices, for example, and for cellular services is rising by re than 35% a year, and creating e hot investment opportunities (page). It's no wonder that cash-rich Brit- Telecommunications PLC, Britain's ne company, has just bet \$1.5 billion the business by buying 22% of aw Cellular Communications Inc., erica's biggest cellular company. n, McCaw has the backing it needs to are off against the seven regional y Bells in a showdown to take over cellular properties of LIN Broadcast- Corp., the nation's most profitable ular operator.

Another example of the opportunities

in phone service: Continued advances in fiber optics and digital switches have big business customers clamoring for more sophisticated transmission networks to handle phone calls and information flow. Indeed, the \$36 billion market for corporate long-distance service will grow more than 12% in 1989, to \$40 billion. So Pacific Telesis, one of the seven regional Bell phone companies, will expand into international service by owning a piece of a transpacific communications cable. If public phone networks can't handle this traffic, then big corporations will build and run their own. Some, such as General Motors Corp., already have. Others are asking the phone companies to do it for them. AT&T, MCI, and Sprint currently are bidding for Merrill Lynch's network contract, said to be worth some \$400 million a year.

In fact, it's surprising how much clout customers have gained in the 1980s. Economic theory says the current trend should work against this—that consolidation eventually kills competition, leading to higher prices and less innovation. Indeed, analysts predict that by the time the dealmaking is over, only five or six multinational giants will dominate the equipment business. And smaller telephone service companies will have merged or formed alliances with communications powerhouses that operate global networks. The negative effects of consolidation aren't showing up yet. Rather,

network equipment is more sophisticated than ever. So is phone service. And it costs less to call: In the U.S., long-distance rates have fallen by almost 39% in the past five years, despite billions of dollars in network improvements and a shakeout among smaller players.

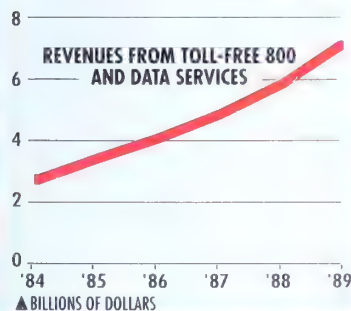
Still, this could change if the industry becomes dominated by a small cadre of multinational suppliers. It took smaller players—such as MCI in long-distance phone service, Northern Telecom in phone equipment, and Apple Computer in personal computers—to spur competition and shake loose innovation at giants such as AT&T and IBM. Moreover, long-distance prices have been dropping primarily because the Federal Communications Commission has repeatedly ordered AT&T to cut rates and keep its profits within a regulated rate of return. Not that anybody's hurting: Leaders AT&T and MCI are reporting record profits, and No. 3 U.S. Sprint should turn its first profit in the first quarter.

LEFTOVERS. Actually, all sides seem happy for the moment. Once, only AT&T offered toll-free 800 service in the U.S. Now its rivals do, too, along with credit-card calling and advanced data transmission that handles everything from facsimile to electronic mail.

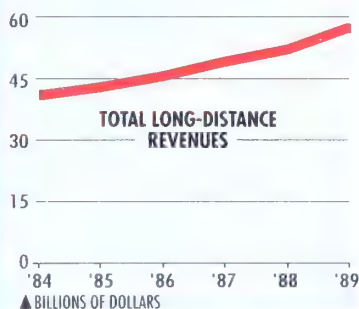
Deals are adding momentum to the spread of improved technology. Carriers such as AT&T and Britain's Cable & Wireless PLC have cut arrangements with carriers in Japan and

...AND BIG OPPORTUNITIES IN SERVICES

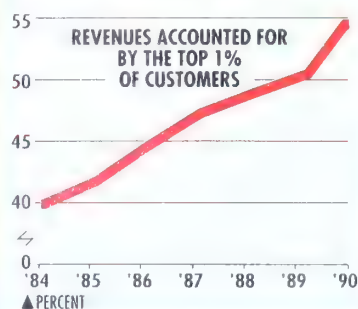
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...IS BOOSTING REVENUES



...FOR COMPANIES IN THE RIGHT MARKETS



DATA: PAINEWEBBER INC.

Europe to operate global voice and data networks employing the latest digital technology. When several of Europe's largest government phone authorities (PTTs) wanted a quick entry into data transmission last summer, they agreed to buy a chunk of Infonet, the international data transmission subsidiary of El Segundo (Calif.)-based Communications Sciences Corp. Other PTTs have had their data networks built by U.S. Sprint's Telenet.

Experience has taught the biggest players that they have to move fast before opportunities evaporate. "You don't want to get stuck with the leavin's," explains E. Wayne Weeks, president of equipment maker AT&T Network Systems. In 1986, for example, Northern Telecom lost to Alcatel the opportunity to buy ITT's international equipment operations—and the French company became AT&T's closest rival for world market share.

An added motivation for dealmaking is the need for partners to smooth overseas expansion. Markets in Europe and Asia are more open than they used to be. With the U.S. and British markets welcoming competition, other countries are following suit. By 1992 the European Community is planning to remove trade barriers and increase competition and innovation by creating a homogeneous market that, like the U.S., is open to all comers. Japan, one of the most restricted markets, is also looking for outside suppliers. Now, British Telecom and Nynex Corp. are bidding to provide a new mobile phone service in Britain. And AT&T has entered the Spanish market through a venture with the national phone company, Telefonica, to make chips.

COMPUTER-GRAMS. Nonetheless, U.S. suppliers still find many markets hard to penetrate. To reverse a \$2.6 billion telecommunications trade deficit, the U.S. is leaning on big equipment purchasers, including Japan, Germany, and South Korea, to open their markets. Last December, President Reagan went to bat for AT&T in Italy, and AT&T won. It's nothing more than other governments do for their companies. In 1987, German Chancellor Helmut Kohl helped derail an AT&T entry into France when it became clear that the U.S. giant had best-

ed Siemens. Ericsson eventually won.

A big problem for most equipment makers—and another reason to deal—is capital: Even the strongest players are straining to push up spending on research and development while prices for their products are falling. In the U.S. alone, local phone companies have spent more than \$20 billion in each of the past five years on switches and transmission lines to maintain and modernize their phone networks. AT&T, MCI, and other long-distance carriers are spending an additional \$5 billion to \$6 billion.

and \$10 billion in cash couldn't save ROLM Corp. Once considered one of the most innovative companies in office phone switches (PBXs), ROLM was losing more than \$100 million a year fighting a price war against AT&T and Northern Telecom. Worse, ROLM's efforts to buy products to market had fallen behind competitors. Now Siemens, which could end up paying as much as \$1.2 billion for ROLM, will get the market share to support product development and try to seat AT&T and Northern Telecom as the world's largest PBX suppliers.

Size is also important because customers want suppliers with staying power. Phone companies want equipment makers that will be around as long as they will. So do corporate customers. And keeping both groups happy requires huge outlays in phone service and equipment R&D. "We're in a long-term business," says Roger P. Kaye, engineering general manager for Hong Kong's Cable & Wireless (HK) Ltd. "The bigger the vendor, the safer we are."

That means a bright future for suppliers with the right customers. Phone companies buy more computerized switches for transmission lines, for instance. They also buy software those switches need to handle new services such as voice mail and advanced billing. That software can cost billions of dollars over several years. Notes a

AT&T executive: "The upfront costs of software design are the same whether you sell to one customer or 1 billion."

This has sparked a bloody battle between AT&T and its foreign rivals to increase market share and cover costs. AT&T is trying to shore up its U.S. power base, which has been eroded by Canada's Northern Telecom Ltd. Now, AT&T has protected its flank by moving to take over GTE's U.S. switch business. That should add greatly to AT&T's 50% U.S. equipment market share, putting it way ahead of Northern Telecom's 15% share of U.S. sales.

AT&T now holds 20% of the world market—but figures that isn't enough. "We think we need at least 25%" to keep profits healthy in the future, says Weeks. European rivals, such as Siemens and Sweden's L. M. Ericsson, have the same idea. Siemens is adding to

SOME BIG DEALS IN TELECOMMUNICATIONS

FEBRUARY, 1988 BellSouth buys Mobile Communications Corp. of America, a cellular phone company, for \$710 million.

JUNE, 1988 United Telecommunications sells its cellular phone operations to Centel for \$772 million in cash, which United uses to buy out most of GTE's share in long-distance phone company U.S. Sprint.

AUGUST, 1988, TO FEBRUARY, 1989 AT&T sets the takeover of GTE's U.S. switch business and joins with Italtel of Italy to supply Italy's \$7 billion equipment market. AT&T also buys Paradyne, a maker of computer communications equipment.

APRIL, 1988 GEC and Plessey of the U.K. combine telecommunications businesses into new entity called GPT, which dominates the U.K. market and owns Florida-based Stromberg-Carlson, a major supplier to U.S. independent phone companies.

NOVEMBER-DECEMBER, 1988 Siemens moves to build world market share by joining with GEC in a takeover bid for Plessey and by acquiring IBM's Rolm, which builds office phone switches.

JANUARY, 1989 British Telecom buys 22% of McCaw, the largest U.S. cellular phone carrier, for \$1.5 billion.

FEBRUARY, 1989 Pacific Telesis will buy 10% of a new transpacific fiber-optic cable, the first to compete with a system run by AT&T and Japan's KDD for international communications traffic.

DATA BW

Companies that can't afford such expenditures need partners. Western Union Corp., the oldest communications carrier in the U.S., has stopped carrying its own telex and business data traffic. Instead, it is leasing transmission lines from other phone companies and betting its future on electronic messaging via computer terminal.

The pressures have forced some equipment makers to merge. ITT started the trend in 1986, when it sold management control of its equipment business to France's CGE. Philips, one of Europe's largest electronics companies, signed over most of its telecommunications business to AT&T. GTE is out, too, having sold or agreed to transfer its various units to AT&T, Siemens, and Fujitsu.

But it takes more than money to succeed. IBM's \$55 billion in annual revenues

world share with sales to several customers. And it could add more joining with Britain's General Electric PLC in a takeover of Plessey Co., 's telecommunications partner. The for Plessey has been put on ice as British government studies it.

VEN AND DIRTY. Nothing better illustrates the war for new markets than the Italian campaign. Italy was probably the huge market in Europe in this century to open its market to new suppliers. Without it, AT&T would end up a second-player on the Continent: Germany is up by Siemens and Alcatel, France Alcatel and Ericsson, and Britain by Plessey and Ericsson.

Once Romano Prodi, chairman of state-owned IRI, Italtel's parent, agreed to negotiate a joint venture with AT&T in telecommunications equipment, the losers charged the Italians with jumping to U.S. political pressure selling out. Siemens, AT&T's only serious rival in Italy, mounted the most aggressive lobbying campaign. It got many to threaten to veto EC approval of huge subsidies to Italy's ailing steel or if Siemens wasn't chosen, according to Italian government sources. And Italian government insiders charged that Siemens was channeling cash to Italian Christian Democratic politicians through allied West German Christian Democrats—charges Siemens denies.

At Siemens was fighting its past. Italtel was a Siemens division before Italianized it, and resentment of Siemens' management style lingers in Italtel and in STET, the Italian phone company. "The Germans are arrogant," says a top Italtel official who asked that name not be used. "It was obvious they wanted to take total control [of proposed joint venture], and we felt there was no way we would be in that position again with Siemens." Siemens refused to budge from its demands. Then, in the final bargaining round, it looked as if AT&T would win,

Siemens relented. It offered Italtel a 10%-to-20% share of a holding company comprising Siemens' European telecommunications interests.

AT&T played hardball, too. A big loss in France the year before had taught it how. AT&T had kept pushing the technical superiority of its equipment to the French PTT, only to get sideswiped by

Robert E. Allen took Prime Minister De Mita aside during his December trip and offered to channel investments such as production plants into De Mita's local political base around Naples. That won over the Prime Minister and "gave him something he could take back to Italy," says an AT&T official.

The deal with Italtel represents a wa-

**AT&T'S WEEKS
NABBED WHAT
MAY BE THE LAST
HUGE MARKET IN
EUROPE WITH
HIS ITALTEL
COUP**



Kohl and the politically astute Ericsson. Just when AT&T thought it was about to clinch a contract for 16% of the French switch market, the Swedish giant won it by cutting a reciprocal deal with the French company Matra to collaborate on building digital cellular phone systems.

In Italy, AT&T mounted one of the strongest lobbying campaigns ever by a U.S. corporation abroad. Several diplomats at the U.S. embassy in Rome worked full-time on the AT&T effort. And President Reagan and President-elect Bush promoted AT&T's cause during key visits to the U.S. in December by Italian Christian Democratic Prime Minister Luigi Ciriaco de Mita and former Socialist Prime Minister Bettino Craxi.

AT&T also offered inducements. According to company insiders, Chairman

tershed in the struggle over who will dominate European telecommunications equipment after 1992. Italy gives AT&T the market share it needs to play a major role in Europe along with a launch pad for marketing new products. And Italy's phone industry will be aligned with the world's most powerful telecommunications company. Moreover, Italy's backward phone company will be able to offer communications service technically competitive with anything in Europe.

Communications service will be the next big battlefield. Encouraged by the benefits that competition has brought to the U.S., Europe and Japan are opening their markets, too. And, like AT&T, carriers such as Japan's mighty Nippon Telegraph & Telephone Corp. (page 144), British Telecom and France Telecom are looking for growth abroad.

The big selling point is networking. A large corporate customer once had to go to numerous communications carriers to set up a global network. But AT&T has joined forces with KDD, Japan's international long-distance company, and British Telecom to offer one-stop shopping. Now any one of these carriers will arrange international links for a corporate customer, plus the necessary network equipment. In residential services, a U.S. affiliate of France Telecom and Southwestern Bell Corp. is testing France's Minitel electronic mail service for Southwestern's customers.

Most of these deals have been friendly. But others could get hostile as foreigners start vying for local-network customers. In Europe, each PTT plans to

**IN ITALY,
PRODI'S TALKS
WITH AT&T
SPARKED A
LOBBYING WAR
PITTING REAGAN
AGAINST KOHL**





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invite in competing mobile-phone operators, having seen the enormous growth that competition has brought in Britain. France has O.K.'d a cellular phone competitor. Germany probably will do the same next month, and some big consortiums are bidding for the rights, including Nynex and such nontelecommunications operators as Daimler-Benz.

U.S. companies, particularly the Baby

Bells, are eyeing this trend hungrily. BellSouth Corp. has agreed to pay \$34 million for the 60% of Air Call Communications Ltd. it doesn't already own, securing its toehold in paging and cellular markets in the U.K., Switzerland, Ireland, Denmark, and Spain. And a consortium led by BellSouth is aiming at the Latin American market. The BellSouth team has cut a deal to build and operate

Argentina's first cellular phone network in Buenos Aires. Another consortium, Eurotel, controlled by Italy's Olivetti and minority partners Cellular Communications and Shearson Lehman Hutton Holdings, is bidding to be a cellular player in Germany and elsewhere in Europe.

But British Telecom's next moves may overshadow all these deals. David Davies, managing director of the company,

JAPAN'S TELEPHONE COLOSSUS TAKES ITS FIRST BABY STEPS OVERSEAS

By any measure, Nippon Telegraph & Telephone Corp. is a sumo-size contender. The revenues of Japan's giant phone company should hit \$45 billion in the fiscal year ending Mar. 31. NTT's \$208 billion stock market valuation is the highest in the world. Its research labs are second to none in Japan. And now it's preparing for a move into global communications.

It may not be a fast move: Tokyo bans domestic phone companies from carrying international traffic. Still, NTT can enter related businesses overseas through subsidiaries. Already, it manages information networks for multinationals and designs "intelligent building" systems that control lights, phones, and computers. A lethargic, state-owned monopoly until 1985, NTT plans to be "a major player on the world scene," says Haruo Yamaguchi, its president since last June.

NTT has to. As its corporate customers set up factories abroad, NTT is trying to hold on to that communications business. It also needs new sources of revenue. Since deregulation, four Japanese carriers have begun cutting into NTT's lucrative phone business. NTT expects a 12.7% drop in pretax earnings this fiscal year, to \$1.8 billion. Its stock has nose-dived to half its 1987 peak price of \$25,238 per share.

SMART SKYSCRAPERS. The chief vehicle for overseas expansion is the four-year-old NTT International Corp., 53% owned by NTT, which mainly consults for government-owned phone companies in Asia. NTTI will break even next year on a 45% gain in revenues, to \$80 million, Yamaguchi says. He's scrounging for growth. NTT's labs recently turned out the HT-11, a handheld sales terminal that NTTI markets overseas. It is made by Seiko Epson Corp. but uses NTTI's software and bears its name. NTTI also is selling an NTT-designed device that splices fiber-optic lines. One customer is AT&T. Product sales, which are now 10% of NTTI's revenues, could



NTT'S YAMAGUCHI: TEAMED WITH EDS

hit 20% eventually, Yamaguchi says.

NTTI also designs and maintains overseas corporate networks, mainly for Japanese companies. And it's in the intelligent building market in the U.S., where it is designing systems for a new, \$80 million Nikko hotel in Atlanta. NTT owns 12.5% of Japan Air Lines Development Co., which owns the hotel jointly with Prudential Insurance Co. NTTI is mulling over several similar projects, some in the U.S.

Eventually, NTTI plans a U.S. company, perhaps to manage groups of intelligent buildings remotely. Another NTT subsidiary is in training for systems integration—installing computer networks. NTT Data Communications Systems Corp. plans to hit the U.S. in the early 1990s with a foreign partner and perhaps NTTI. To learn American business culture, it has teamed with Electronic Data Systems Corp. to do systems integration in Japan for such

American-owned companies as Citibank and Salomon Brothers Inc.

NTT Data dominates its home market partly because it is independent of Japan's big banking and industrial groups, or *keiretsu*. For example, NTT Corp., a member of the Sumitomo group, is at a disadvantage when bidding on systems integration work from competitors of Sumitomo. Spun off last July, NTT Data expects to post revenues of \$1.7 billion for the nine months ending Mar. 31. Overseas, "NTT Data would be an extremely powerful rival in systems integration," says Shintaro Maeda, a manager at NRI & NCC Co., NTT Data's top rival in Japan.

RELUCTANT SHOPPER. Obstacles remain to NTT's rapid overseas expansion. It lacks marketing expertise. And a splashy move might set off political alarms. U.S. trade officials already grumble that NTT is slow meeting its 1981 promise to buy more American-made equipment. At home, the Postal Telecommunications Ministry soon will probe the phone giant's subsidiaries during a review of deregulation—barring if NTT is anticompetitive.

So sensitive are things that the Recruit Co. stock scandal has revived calls for the phone company's breakup. An aide to former NTT Chairman Hashi Shinto had deposited \$70,000 from the sale of shares of a Recruit subsidiary in Shinto's bank account. The fair forced Shinto's resignation in December—which could hamper overseas expansion. Says President Yamaguchi: "He was the only top executive who had great experience in international activities."

Most observers, however, call the Recruit affair a temporary setback. Gradually, as NTT's domestic competitors expand, the phone company will gain a freer hand abroad. NTT "is wide awake but hasn't stood up yet," notes Yamaguchi. When it does, it's likely to cast a giant shadow.

By Amy Borrus in Tokyo



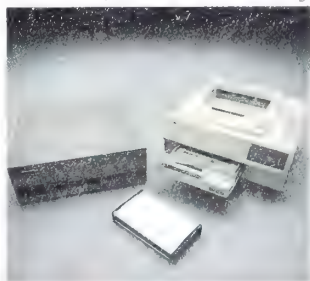
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PHONE STOCKS: SHOULD YOU PLUG IN OR DISCONNECT?

Telecommunications sent Wall Street some of its biggest winners last year, particularly the emerging cellular-service companies. This year, the industry is likely to be a source of more bonanzas, according to investment pros. And the prospects—and reasons—for mergers, joint ventures, and other deals have a lot to do with their thinking.

Equipment makers—the ones dealing from weakness—are everybody's dogs. Based on their risk-adjusted potential, most telecom-equipment shares are fully valued and expected to be poor performers in the next 12 months, according to a recent industry survey by Value Line Inc., a research company. Among such stocks: ADC Telecommunications, Gandalf Technologies, Mitel, and Northern Telecom.

LONG LINES. But stocks of service companies—those that carry phone calls and data—are a different story. "There are still a number that offer terrific values," says investment manager Joan Lappin, president of Gramercy Capital Management Corp. Takeover talk spurred moves of 35% to 50% in the hot cellular stocks in 1988. This year, big investors seeking those types of gains are placing their bets on established carriers.

Except for American Telephone & Telegraph Co., which is on few buy lists for fear that its revenue-growth potential is limited, "most large telephone company stocks are 20% to 30% below their reasonable market values," argues Charles W. Schelke, telecommunications analyst at Smith Barney, Harris Upham & Co. Lappin's favorite is MCI Communications Corp., now at 24. MCI "has turned cash-flow positive" after years of having to sell securities to meet its expanding demands, and Lappin is looking for its stock to reach the upper 30s this year.

One burning question is how to view the Baby Bells—market laggards in 1988 and again so far this year. Schelke likes them best. He forecasts 20% to 30% market appreciation within 18 months, partly because he expects a change from rate-of-return regulation to limits on prices—letting the Bells boost annual profits by 3% to 5%, he says, as they cut costs. Moreover, the Bells generate huge amounts of cash that could be used to buy back shares. Schelke's favorites: Southwestern Bell,

currently trading at 43; Pacific Telesis, now at 33; and Nynex, at 67.

A darker view is taken by Value Line analyst Helena Openshaw, who says: "None of these companies is expected to outperform the averages in the next six to 12 months." She notes that government regulation has limited the Bells' diversification efforts so much that their nonphone operations "are not big enough to materially boost profits or the stock price."

Openshaw prefers independents with cellular, paging, and cable operations. Her favorites are C-Tec, Cincinnati Bell, and United Telecommunications,

POISED TO RISE?

The following telecommunications stocks were the ones most favored in a recent BW canvass of money managers and industry analysts

Stock	Recent price	Target price*
BELL ATLANTIC	\$73	\$100
BELLSOUTH	40	70
CENTEL	63	113
MCI COMMUNICATIONS	24	48
NYNEX	67	98
PACIFIC TELESIS	33	60
SOUTHWESTERN BELL	43	80
TELEPHONE & DATA SYSTEMS	36	50
UNITED TELECOM	48	65
U.S. WEST/NEWVECTOR	29	40

*Peak price analysts expect for 1989

which has acquired U.S. Sprint from GTE. She also argues that though takeover rumors have pushed up telecom stocks, "there is a special element of risk to playing the takeover candidates"—mainly regulatory constraints on hostile takeovers.

That's not so worrisome to Joel D. Gross at Donaldson, Lufkin & Jenrette Securities Corp. He notes that regulatory hurdles don't often apply to industry insiders. "Phone companies have been buying other phone companies on a friendly basis for 50 years," Gross notes. Regulators are less anxious about changes of ownership in such cases, he adds. He's banking on more friendly deals to boost his picks, such as Bell Atlantic, BellSouth, United Telecom, and Telephone & Data Systems—and to make 1989 a good year for most telecommunications stocks.

By Gene G. Marcial in New York

Communications Systems Div., says in acquisitions of niche players such as voice-mail operators and Metrocast. U.S. paging company, will hardly meet his goal of becoming "the world's most successful telecommunications company." Buying Mitel Inc., the fifth-largest supplier of PBXs, hasn't helped much either. The powerful Siemens-ROLM combination couldn't have come at a worse time for Kanata (Ont.)-based Mitel, which is losing market share and money. So over the next 18 months, British Telecom will chase more big deals in the U.S. And it will make big investments in European companies that offer speed of data and management network services. Says Dey: "We won't be the nice guy saying we're not going to get involved."

NO BENCHWARMING. Neither will the Baby Bells. The seven companies have stepped up their fight to have Congress release them from AT&T's broad agreement with the U.S. district court in Washington, which prohibits them from manufacturing equipment, owning and selling information services, or selling domestic long-distance service. AT&T's former phone companies have received permission to buy into overseas cellular phone operations and non-phone businesses. For instance, Nynex has purchased the software company Group of England. Still, "we have to be more aggressive," says Nynex Chairman Delbert C. Staley. "We can't wait for a company like British Telecom to come over and take away our business." Adds Ameritech Chairman William L. Weiss: "You're telling seven huge companies to sit on the sidelines."

That's not always bad, as some of the zealous competitors have discovered. But thought ROLM would make it competitive with AT&T and Northern Telecom in office phone switches. But Big Blue got burned—just as AT&T has in trying to match IBM in computers. Now real deals will help both companies zero in on what they do best. "So many companies that have been to Oz are finding out there's no place like home," says Robert B. Morris III, telecommunications analyst at Goldman, Sachs & Co.

That's the challenge as competition heats up: to grow fast without losing control. It's a skill that many players will have to learn soon—or risk being left behind.

By John J. Keller in New York, John Rossant in Rome, Mark Maremont in London, Thane Peterson in Paris, and Tier in Atlanta, and bureau reports

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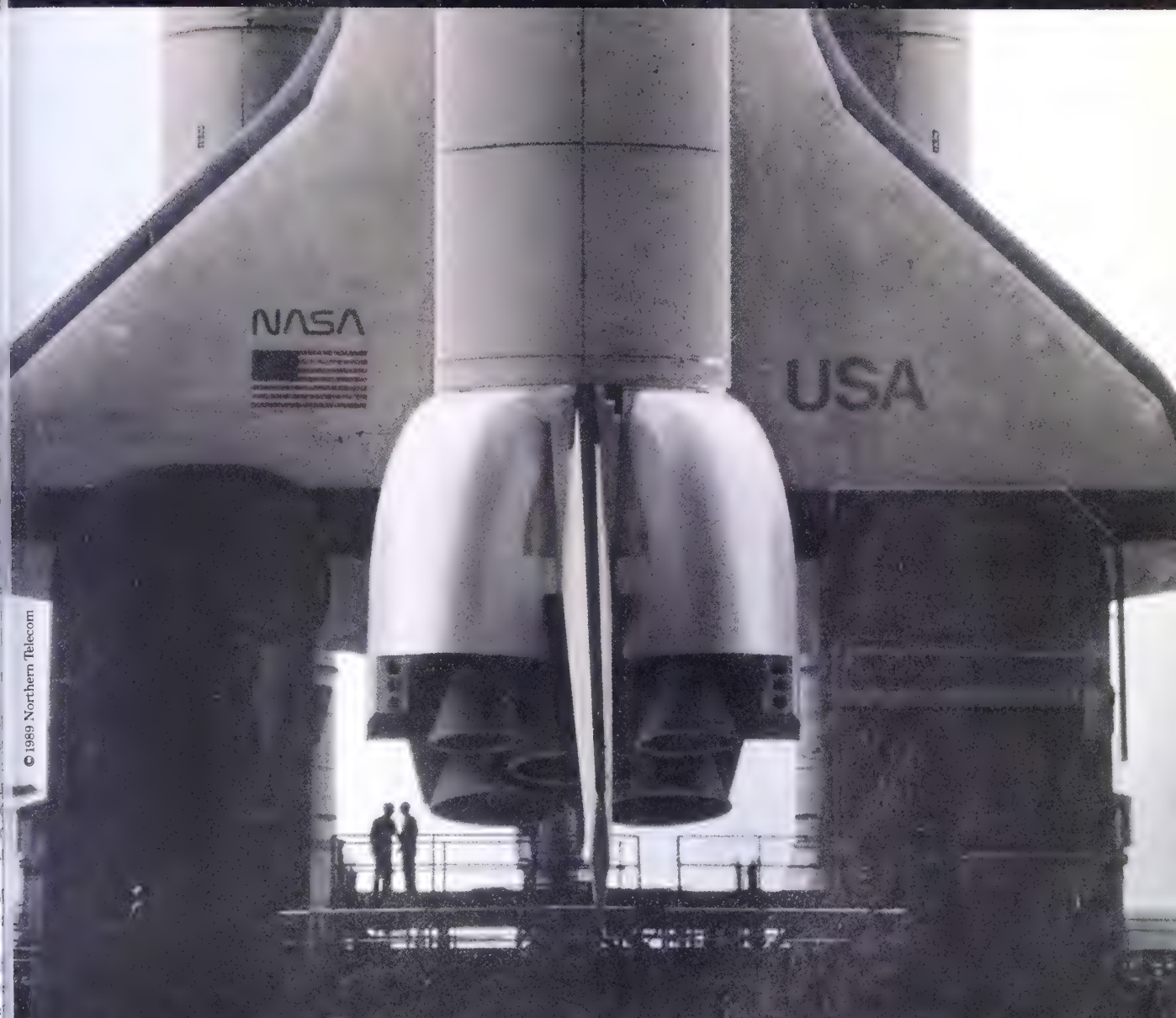
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WEEKEND TOURNAMENTS PROMOTE SUCH LUXURY ITEMS AS ROLEX WATCHES AND CADILLAC

The brilliant Florida sun glints on the Rolls-Royces, Mercedes-Benzes, Porsches, and Cadillacs in the parking lot of the Palm Beach Polo & Country Club. On the field, a horse gallops toward the goal as its rider thwacks the ball with his mallet. Many of the audience of 3,500 are on their feet, champagne glasses in hand. But the shot misses, and The Franklin Mint Sterling Cup Final ends with the score 8-7. The winning players receive jeweled Fabergé eggs from The Franklin Mint. And the company, which sells its pricey collectibles by mail, hopes its first polo sponsorship is also a winner.

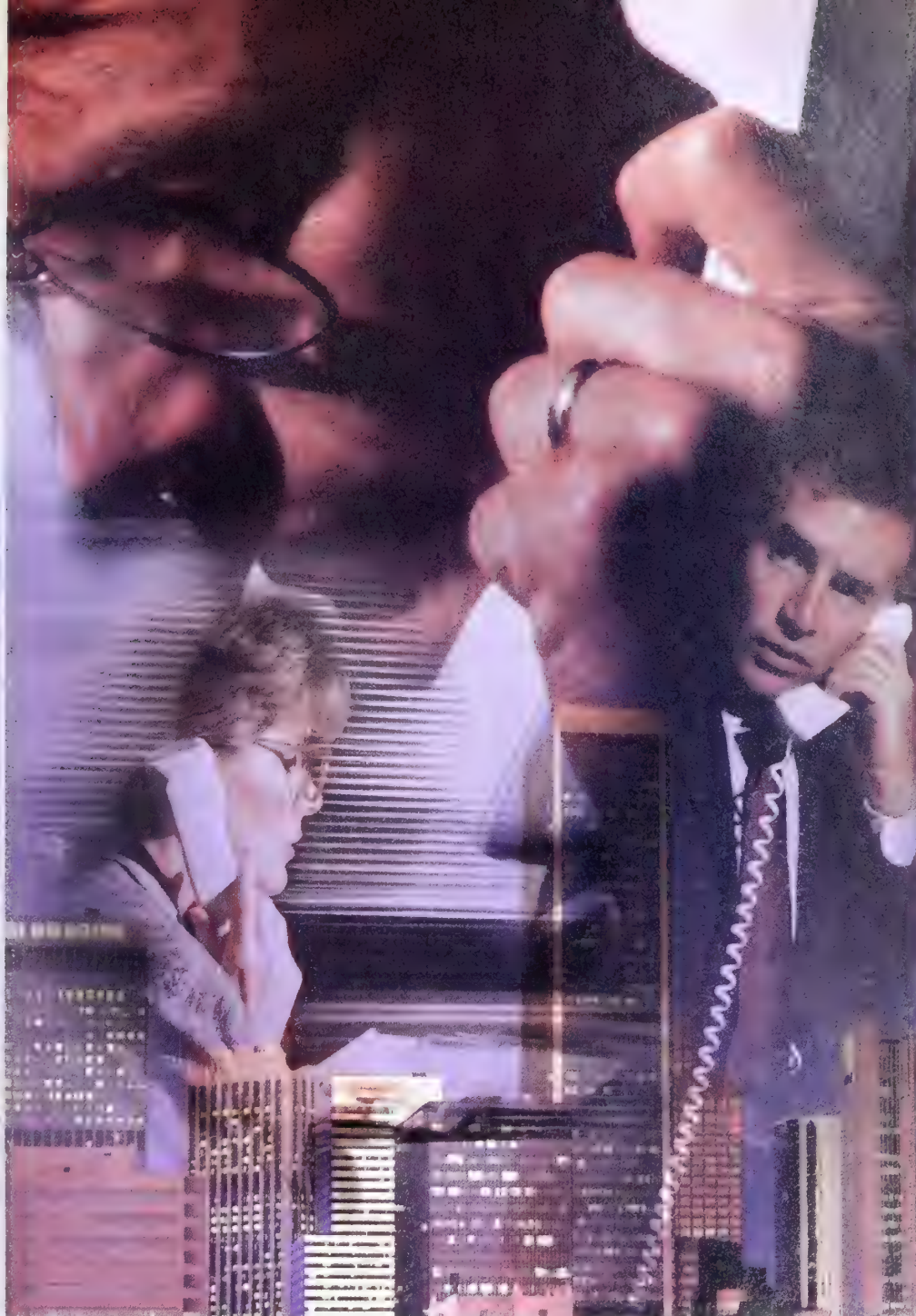
It's no secret that corporate association with polo has long been an efficient way to target a wealthy audience. Just pick up a program at a match and skim the ads for luxury cars and super-expensive watches. But now companies selling everything from cellular telephones to health club memberships are trying to cash in on polo's cachet and join the likes of Cadillac, Cartier, Rolex, and Ralph Lauren, the designer who uses Polo as a brand name. From virtually nothing a decade ago, companies now pony up an estimated \$25 million a year to sponsor polo tournaments and teams. "Polo is about style, quality, taste, beauty, and

elegance," says Cartier Inc. Chairman Ralph Destino. "The affinity appeals."

So do the demographics. Polo audiences are small: about 5,000 tops for most tournaments at the Palm Beach club, for example, rising to 8,600 when Prince Charles played there on Feb. 1. But with the polo crowd, quality counts more than quantity. About half of polo devotees have a household income of at least \$100,000 and a net worth of \$500,000 plus. Polo is about as far as a tractor pulls as you can get.

DIVOT STOMP. Indeed, tailgate parties with expensive picnic hampers and beer tail shakers are *de rigueur* at the Palm Beach club, Royal Palm Polo in Boca Raton, Fla., and other clubs. And as a part of the tradition, spectators happily stomp onto the field between the third and fourth chukkers, or playing periods, to stomp down divots.

As for the players, they're not just the Prince of Wales and a bunch of Argentinians, who are generally perceived as the best in the sport. Polo, with roots in ancient Persia, is now played in more than 60 countries. In the U.S., there are 255 polo clubs with their own membership rosters, and membership in the U.S. Polo Assn. is up 73% over the past five years, to 2,600. Charles R. Kees



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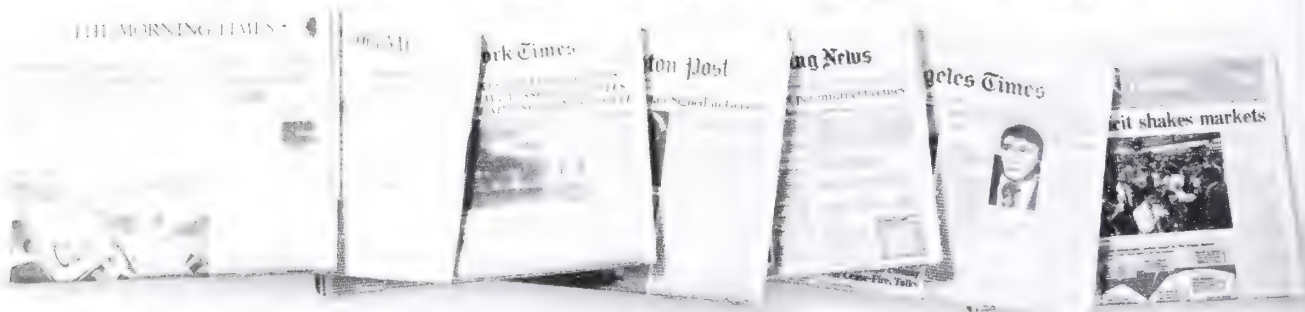
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(All Times Eastern)	1st 1/2 hr	2nd 1/2 hr	3rd 1/2 hr	4th 1/2 hr
Top Business News	6:30	7:00	7:30	8:00
Financial News	6:35	7:05	7:35	8:05
Small Business News	6:40	7:10	7:40	8:10
Special Business Features	6:50		7:50	
CEO Close-Ups		7:15		8:15
Internat'l Business Line		7:25		



1989 EXECUTIVE EVENTS

SEMINARS

Strategic Planning for New Technologies

Technology can give your firm a sustainable competitive advantage. How can you make certain your technology investment delivers this advantage? Business Week's Executive Seminar on Strategic Planning for New Technologies will show you how to maximize the return on your technology investment.

■ February 14, New York ■ February 23, San Francisco
 ■ March 7, Chicago ■ March 16, Boston ■ April 6, Miami ■ April 19, Toronto
 ■ May 11, New York

Shareholder Value Creation

Stock price performance has become an overriding concern in today's corporate climate. The Business Week Seminar on Shareholder Value Creation explores how your company can achieve superior stock price performance relative to the market while avoiding unwanted investor actions.

■ February 9, New York ■ February 16, San Francisco
 ■ February 27, St. Louis ■ March 6, Boston ■ March 14, Miami ■ March 21, Washington ■ April 4, New York ■ April 17, Chicago ■ April 27, Cleveland

Sales Forecasting: How To Predict Demand

Accurate prediction of future sales can make the difference between success and failure for any product or service. By using the latest predictive techniques, executives attending this Business Week Seminar will learn to forecast sales with clarity and vision. A joint presentation of Business Week and DRI/McGraw-Hill.

■ March 9, New York ■ March 14, Los Angeles ■ March 21, Boston
 ■ April 4, Chicago ■ April 11, Stamford, CT ■ April 18, Toronto
 ■ April 25, Minneapolis ■ May 16, San Francisco ■ May 23, New York

Lifestyle Marketing: How to use sports and other live events to reach your market

Sports and other public events are becoming effective marketing vehicles with the power to break through media clutter and reach a target audience. Business Week and Del Wilbur + Associates present this seminar to provide marketing professionals with the sophisticated techniques they need to create and manage effective event marketing programs.

■ Spring

SYMPOSIA

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■ March 7-8, New York

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■ May 2-3, New York

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president of Technology Funding Inc. a venture capital firm in San Mateo, Ca. started playing four years ago. With year he had bought three horses now has a stable of nine. Michael Tarnopol, a managing director of B Stearns & Co. who took up the game years ago, now captains a team sponsored by Revlon Inc. The speed and are exhilarating, says Tarnopol.

ELEPHANT POLO. But enthusiasts believe polo will never achieve mass appeal until it becomes a professional sport, which seems unlikely. The narrow audience means limited TV exposure, which so has been restricted to CBS Inc. featuring America's Polo Championships and specials on ESPN and SportsChannel. Scant TV coverage, however, keeps a marketing bargain. Tournament sponsorships can be had for as little as \$35,000, though many invest much more. Cartier has spent more than \$1 million for polo matches. Besides those in Florida, it sponsors regular matches in Britain and Mexico. It also sponsors

Scant TV coverage keeps polo a marketing bargain. Tournament sponsorships cost as little as \$35,000.

time events such as elephant polo in Nepal and a match this year in the wealthy sultanate of Brunei.

Cadillac's role as official car of the Palm Beach Polo Club and sponsor of the \$100,000 Cadillac World Cup has been so successful that Toyota Motor Corp. is following suit. It is sponsoring the Open Polo Championship in Lexington, Ky., as part of the introduction of Lexus, its \$35,000 luxury sedan. Rolex has expanded its sponsorship of the Rolex Gold Cup and the Rolex/Abercrombie & Kent team to other events, including two matches in which Prince Charles is scheduled to play. Abercrombie & Kent is a deluxe tour packager.

As for Ralph Lauren, his link to polo has become a legal wrangle. His company began benefiting from polo's prestige more than 20 years ago, thanks to Lauren's famous silhouette of a horseman swinging a polo mallet. Some players feel that, as a consequence, he should have given the sport more financial backing. Instead, when the U.S. Polo Assn. tried licensing its own, similar logo four years ago, Lauren sued, citing trademark infringement. The suit is now being settled amicably.

By Gail DeGeorge in Palm Beach County

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Finances

HOW LONELY BROKERS ARE REWRITING THE BOOK ON SERVICE

It's a different scene at Fidelity Investments these days. Two years ago, if a would-be investor called, phone representatives would have tried to sell something—usually the hot fund of the month. Now, however, they discuss your portfolio, trying to assess “your postcrash recovery profile,” says Susanne Mahoney, vice-president for retail marketing. And the information they send you may well be about precious metals or life insurance or even certificates of deposit—instead of the volatile sector mutual

funds that once dominated Fidelity's offerings.

Fidelity isn't the only brokerage that is coddling customers more these days. Of course, efforts like investment seminars, 24-hour account information hot lines, or redesigned account statements may be mainly cosmetic. Few houses are going so far as to cut their commissions. Still, they're doing just about anything else to win back business.

Some firms are enhancing their asset-management accounts—brokerage accounts

tied to a money market fund that has check-writing and charge-card privileges. Many are gilding the plastic by offering gold Visa or MasterCard for a \$25 annual fee instead of the usual \$35.

A BIT OF FLOAT. Unlike bank cards, brokerage cards are actually debit cards: Purchases don't go on a monthly bill but get immediately subtracted from your account. Now, though, some firms delay the debiting until the end of the month, allowing you a bit of float.

Other new products serve

to make a mutual fund investor's life a little more convenient. Under Fidelity's delayed-dividends program, investor's earnings from a mutual fund can be reinvested automatically into another fund. And Merrill Lynch, under a dual-pricing program introduced last November (ENR Oct. 31), lets you choose to pay fees either up front or at redemption.

As part of the mandate to develop a financial-consumer role, brokers are catering to investors' passion for short-term vehicles.

are actively promoting certificates of deposit (CDs), a commission-free product. Typically, each week a broker offers 15 to 25 fixed-rate loans from midsize banks and savings accounts around the country. The national scope of the program gives investors a chance to participate in a yield that could be higher than hometown rates. And because brokers make a market in these investments, investors can withdraw without penalty (though prevailing market rates may mean you may get less than value).

TURNERS ONLY? Another service-oriented enhancement is personalized portfolio management for accounts of at least \$100,000. Clients discuss their investment goals and philosophy with the broker, then choose among several independent money managers screened by the firm. The manager receives full discretion to trade on your behalf. The annual fee—usually 3% of assets—“wraps in” the manager's fee and all broker commissions.

It's steep—\$9,000 a year, for example, on a \$300,000 portfolio. A money manager acting on your own is likely to charge only about 1%, so to get these “wrap accounts” you'd have to be running commissions of more than 1% a year. That's enough to cover several dozen trades. Wrap accounts can be costly, your manager prefers a hands-on approach. Some firms, like Prudential's “managed assets consulting services,” do scale the percentage as portfolio size mounts: 2.5% for assets from \$500,000 to \$1 million, 1% over \$5 million.

Wrap accounts offer a convenient way to locate a reliable manager: “Often, people wouldn't take initial accounts [of \$100,000],” says John Steffen, CEO of Merrill Lynch Prime Markets. But make the brokerage's periodic reporting includes a performance analysis that evaluates the portfolio's earnings in relation to general market conditions, stock indexes, and other

managed portfolios—not just a quarterly statement saying: “Your account was up 3%. The S&P 500-stock index was up 4%. Have a nice day.”

Brokerages are also offering real estate limited partnerships, and theirs are often safer than those from independents, says Christopher

Davis, chairman of the Investment Partnership Assn.: “They make these deals jump hurdles higher than anyone in the industry.” Even so, you should evaluate the track record of the managing partner.

Of course, brokerages have an ulterior motive in all these diverse services: To capture

your assets with something conservative today, in hopes of rolling them over into something more aggressive tomorrow. But look past the hype, and you may find that some of these investment sweeteners are more than quick pick-me-ups for your portfolio. *Troy Segal*

Investing

RAISING ARABIANS CAN HAVE YOU ROLLING IN CLOVER



BEAUTY CONTEST: “LOOK,” PEDIGREE, AND FERTILITY ARE KEY

Arabians. They're the grand elite of the equestrian world—an ancient breed that traces its origins back to the Pharaohs. There is an undeniable romance surrounding these majestic horses, whose beauty and grace have long made them prized possessions among royalty and the ultra-rich. Such business and entertainment celebrities as Occidental Petroleum Chairman Armand Hammer, financier David Murdock, singer Wayne Newton, and actress Jane Fonda are all admitted Arabian addicts.

But you don't have to be a celebrity to own an Arabian. Show-quality horses are available for as little as \$25,000. Arabian prices plunged by as much as 75% after the heady days of the early 1980s, when several horses fetched more than \$1 million. But experts say the market, while still

sluggish, is unlikely to fall further. At the recent Scottsdale Arabian Show in Arizona, the main event in Arabian horsemanship, only three horses auctioned for more than \$100,000. Prices are about the same as last year.

SHOWTIME. Investing in Arabians is different from putting money into almost any other breed. Arabians aren't really racers: Although some small races have been organized, Arabians are primarily show animals. So the way to make money with them is through breeding, a process in which illness or infertility could wipe out your investment.

The first thing you'll need to do is find a reputable farm. The one you select should be a proven producer, in business at least 10 years, and should provide long-term support, such as breeding and promotion services. Visit horse shows or seminars and

make contacts. Magazines (*Arabian Horse World*) and newsletters (*Arabian Horse Journal*) can help you see who's producing winners in the show ring.

You'll probably want to start with a proven mare; fillies are cheaper but less predictable. Investing in stallions isn't for beginners: Only 4% are quality breeding stock, and a horse's price is determined by reproductive ability as well as by its pedigree and conformation, or “look.”

Buy the best horse you can afford, even if it means taking in partners. Your chances of getting high-quality offspring are that much greater. Experts advise sticking with “purebred” Arabians—those with ancestors from one country, say Egypt, Poland, Spain, or Britain. Those with mixed blood usually sell for much less but don't have the cachet of the purebreds.

Expenses will run \$5,000 a year or more, but then, breeding horses can be a business. Make money at it in two years out of seven, and most expenses become tax-deductible. You can depreciate the horse over 5 years if it's under 12 years of age, or 3 years if it's older.

The payoff can be substantial. Donald Saluti, a retired commodity executive, bought a pregnant mare in 1980 for \$180,000. The resulting filly later bore five foals that he sold for nearly \$500,000. He sold the second mare for \$200,000 in 1987. Saluti has since bought several other horses. When he's not making the show circuit, he's out at his farm with his two grandchildren—who have grown attached to the horses. “It's the perfect family experience,” he says. “I wouldn't trade it for anything.” *Mark Ivey*

Smart Money

TAKING THE TEETH OUT OF A NEW TAX BITE

If you've been counting your blessings because you've heard there are no new taxes in 1989, well, read our lips. As of January 1, taxpayers 65 or over face a catastrophic illness insurance premium—in effect, a brand-new tax meant to finance a major expansion in medicare benefits. But for those planning ahead for a retirement some years off, as well as for the already retired, there are a couple of ways to lighten the burden of this new tax.

The medicare surcharge is based on the amount of income taxes you pay. For every \$150 of taxes due on 1989 income, anyone eligible for medicare—all those at least 65—must pay an additional \$22.50. The surcharge,

7.5% yield, they would owe \$8,852 in income taxes and \$1,328 for the medicare surcharge, for a total of \$10,180, a difference of \$895. "The surtax is very hard to eliminate. But muni bond funds are a way of reducing the overall size of the surtax," says Neal Litvack, vice-president for marketing at Fidelity Investments.

The other option is to defer taxable income by investing in an annuity, a long-term, tax-deferred contract issued by an insurance company. With a variable annuity, the money can be invested in a mutual fund. Holders have different withdrawal options, including a guaranteed lifetime income. The idea is that the money can grow during an "accumulation phase" without being taxed. When the annuity enters the "payout phase" and withdrawals become taxable, there's a good chance the annuity buyer will be in a lower tax bracket.

Even for people who remain in the top bracket after retirement, there is a plus—taxes are paid only on the earnings taken out, while continuing growth of the principal is sheltered. "You can increase your spendable income by close to 50% with a variable annuity," declares Eleanor Etter, director of marketing for Fidelity Investments.

And remember that taxpayers are getting new benefits in exchange for the new tax. It used to be that even for a prolonged illness, medicare would pay for no more than a 120-day hospital stay. Now, Congress has extended medicare coverage indefinitely. The only hitch is that all older taxpayers now have to pay for the new benefits, whether they want them or not. *Leah Nathans*

Tax-free munis can ease the catastrophic illness premium

a steep 15%, is capped at \$800 per person or \$1,600 per couple this year, but it will be set higher in the future.

The only way to ease the sting of the catastrophic illness premium is for taxpayers to reduce their taxable income. One way is to invest in tax-exempt municipal bonds.

ANNUITY OPTION. Take the example of a married couple over 65, with \$45,000 in taxable annual income and \$35,000 to move into a non-taxable investment. If they invested the \$35,000 in a taxable bond fund with a 9% yield, they would owe \$9,630 in income taxes and \$1,445 for the medicare surcharge, for a total of \$11,075. If they invested instead in a tax-free bond fund with a



Travel

MISS THOSE FREQUENT-FLYER DEALS? TRY CARRYING A POUCH

At \$6,420 for a New York-to-London round-trip ticket, a flight aboard a British Airways Concorde does seem to be a bit of an extravagance. But what if you could take the same luxury flight for a mere \$820? You can if you're willing to be a courier.

It used to be that only college students and other infrequent or relatively impecunious fliers would deign to serve as international couriers. But with frequent-flyer discounts harder to come by these days, business and vacation travelers are reaping big discounts by delivering such things as canceled checks, blueprints, and other small cargo for courier services.

Most services are booked at least two weeks in advance. But they send couriers almost daily, so you should have little trouble signing up. On the day of the flight you'll be met at the airport by a courier agent who will hand you your ticket, check you in, and give you printed instructions on what to do when you land. You'll get your pouch, which you'll carry aboard or, if it's large, check as luggage. Reputable services will tell you the kinds of things you're carrying. At customs you'll go on a special line for couriers.

Your own luggage is usually restricted to what you carry on the plane. But it varies among courier companies. When you arrive, an agent will meet you and you through customs on the other end.

A DEUX. Here's a rundown of some popular services: Skypack (516 745-6656) offers round-trip Concorde flights to Europe. Because of heavy demand, it's best to book on the Concorde at least 10 months in advance. TNT book a flight for you and a companion to both travel couriers. TNT also offers Concorde round trips to London for \$450, Rio de Janeiro for \$550, and Dublin for \$650.

IBC, one of the world's best couriers (718 262-8052, 213 216-1637), goes from New York to most European cities, plus Milan, Düsseldorf, and Rio. From Los Angeles IBC offers round-trip flights to Hong Kong, Singapore, Tokyo, and Seoul for \$350, to Taipei for \$250. Mayday International (213 410-6721, 1100) offer round-trip flights from Los Angeles to London for about \$400.

As an added bonus, many services will allow you to keep the frequent-flyer miles you accumulate. *Pat*

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Not so long ago, adding moisture to the air in your home meant putting a pan of water on the radiator. Then came electric steam vaporizers, cool-mist impellers, and finally, sleek "ultrasonic" humidifiers that have been promoted as quieter, safer, and more efficient.

But government studies are beginning to highlight potential health problems with even the most high-tech and expensive of the devices, which are priced from \$69 to \$199. Underneath their snazzy exteriors, they are machines that demand some rather grubby, and very diligent, maintenance. Unless you use and clean them properly, they can become breeding grounds for bacteria and viruses.

Ultrasonic units made by such companies as Toshiba, Bonaire, Welbilt, and Sunbeam have won high marks for overall performance. They contain so-called nebulizers that use sound waves to break water up, silently hurling the tiny droplets into the room. They can run from about 8 to 36 hours without refilling, depending on the machine's size and the intensity of the mist.

WHITE DUST. Although Toshiba's model is one of the most efficient, it lacks a feature common to Bonaire, Sunbeam, and several other brands: disposable filters. Such cartridges are a must if you live in a hard-water area such as Chicago. Otherwise, ultrasonic humidifiers deposit a fine layer of white dust, which is composed of pulverized minerals from the water, all over the house. The filters, which cost about \$10 apiece, typically last a winter season. But in regions where the water is heavily laden with minerals, they must be replaced as often as every two weeks.

Health

IS YOUR HUMIDIFIER HAZARDOUS TO YOUR HEALTH?

Filters may limit the white-dust problem, but the Environmental Protection Agency has discovered another unsettling side effect. The humidifiers appear to raise the levels of airborne particles in the house dramatically, sometimes to as high as 10 times the federal standards of acceptability. The ultrasonic waves do appear to kill bacteria lurking in water. But unlike other cool-mist machines that simply spray water through a fan, the ultrasonics combine any bacterial residue and mold with lead, asbestos, or other pollutants—and then spew that mixture around.

Concerns about that brew prompted the Consumer Product Safety Commission to issue a warning in December urging consumers to use distilled water, empty the devices completely between uses, and clean them frequently.

The manufacturers don't quibble: "If you left a glass of water on your desk, you wouldn't come back and drink it tomorrow," says John McEvily, president of Bonaire Corp.

Unfortunately, by the time you use distilled water and buy the cartridges, the supposed convenience of these ultrasonic systems begins to fade. That's why some homeowners

still prefer vaporizers. The key advantage: Boiling the water purifies it. The EPA has found that these devices do not raise particulate levels. Manufacturers such as Sunbeam and Pollenex have replaced old-fashioned, glorified tea kettles with sleek units selling for \$50 to \$100.

CENTRAL PLANNING. If a portable humidifier isn't meeting your needs, you can have a more elaborate system made by Honeywell, Lennox Industries, Carrier, or others hooked up to your central heating-and-ventilation system by a contractor. Expect to pay \$400 or more, depending on the size of your house and local humidity levels.

Almost all central humidifiers are tied into the plumbing system for a steady water supply. But their designs

vary greatly. Some older models are much like the radiator pan of yore, except that use evaporation tanks that inside a warm-air duct the furnace. These systems must be cleaned at least every two weeks, since water sitting in the tank could become contaminated by bacteria. New models work on the principle as the ultrasonics spraying atomized water into the airstream from your furnace. The flow is controlled by a humidistat that senses the moisture level in the air. Such models usually require only seasonal maintenance.

The EPA is testing the particle levels emitted by these devices. But what those studies show, since central systems draw their water directly from the intake plumbing, they may not be advisable if your water is high in minerals content.

Joan O'C. Hamilton

Worth Noting

■ **WHEEL DEAL.** If you think your old car is worth more than a dealer offers, check the "cars wanted" classifieds. Some charities solicit car donations for which you

get a book-value tax deduction. Among them: Jewish Institute for the Blind (212 532 4155), which wants vehicles that are less than seven years old, and Volunteers of America (800 462 1715).

■ **JEWELS FOR HIRE.** Nobody wants to wear the same

\$10,000 sapphire bracelet forever, right? Well, Salon Metro in New York (212 983-3636) will lease precious bijoux for \$35 to \$5,555 a month, including insurance, depending on their value.

■ **HEALTH HELP.** If you're self-employed, don't forget

to take advantage of a break awaiting you on your 1988 tax return: 25% of premiums you paid for health and disability insurance for you and your immediate family is deductible in 1988, according to accountants at Arthur Andersen.



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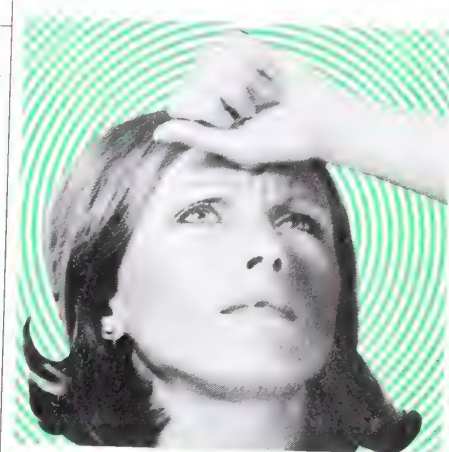
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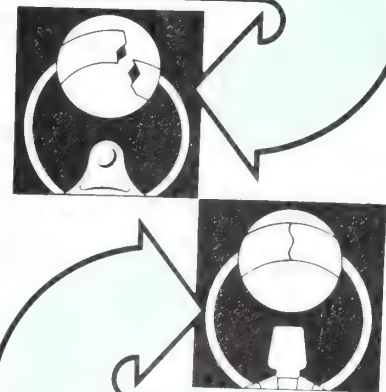
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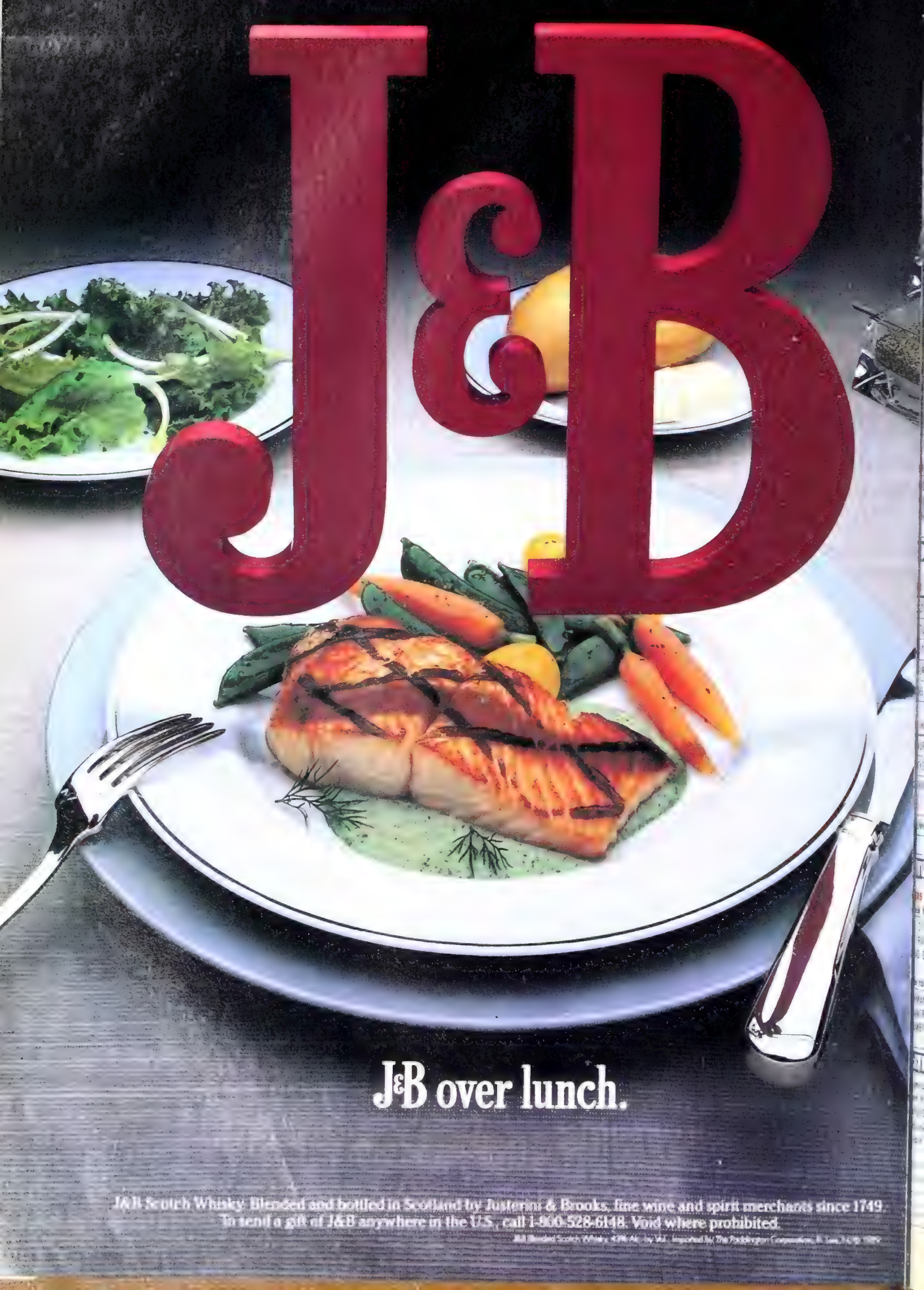
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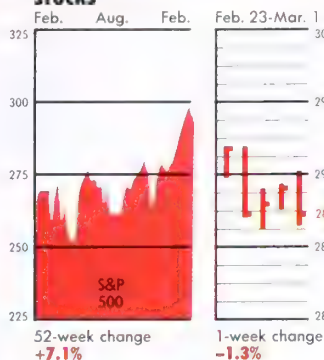
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Investment Figures of the Week

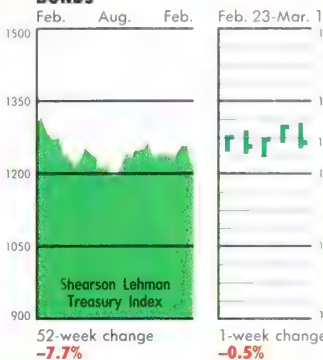
SENTARY

Stock market's miasma continues as interest rate jitters sent equities tumbling on Feb. 24 and Mar. 1. Followers of small-capital stocks took heart, as sector stocks suffered less than the S&P 500. Interestingly, gold prices fell below \$390 an ounce, despite the upturn in rates. The realigning by foreign investors, spurred by a rise in the dollar, and the technical indicators, including a call ratio of speculative interest, which had been negative, suggest a neutral outlook.

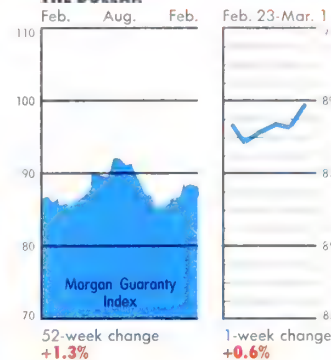
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS	Latest	% change	
		Week	52-week
INDUSTRIALS	2243.0	-1.8	8.3
COMPANIES (Russell 1000)	152.3	-1.1	7.4
COMPANIES (Russell 2000)	154.7	-0.5	12.6
COMPANIES (Russell 3000)	163.7	-1.1	7.8

INTERNATIONAL STOCKS	Latest	% change (local currency)	
		Week	52-week
FINANCIAL TIMES 100	2021.3	-0.6	11.8
NIKKEI INDEX	31,964.3	-1.1	24.5
TSE COMPOSITE	3551.6	-0.9	10.0

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	8.6%	8.5%	5.6%
30-YEAR TREASURY BOND YIELD	9.2%	9.1%	8.3%
S&P 500 DIVIDEND YIELD	3.3%	3.4%	3.1%
S&P 500 PRICE/EARNINGS RATIO	11.6	11.8	15.4

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 26-week moving average	278.5	277.4	Positive
Stocks above 26-week moving average	59.1%	65.7%	Neutral
Speculative sentiment: Put/call ratio	0.30	0.24	Neutral
Insider sentiment: Vickers sell/buy ratio	1.15	1.03	Positive

INDUSTRY GROUPS

WEEK LEADERS

	% change	
	4-week	52-week
MINING	12.9	20.4
PRODUCTS	12.8	77.0
HEALTH CARE SERVICES	9.4	-34.4
RECREATION	6.5	15.3
TELECOMMUNICATIONS	3.7	-26.7

WEEK LAGGARDS

	% change	
	4-week	52-week
MANUFACTURED HOUSING	-9.5	31.6
TECHNOLOGY	-8.3	3.1
TOOL & DIE	-6.5	-4.4
TRANSPORTATION	-5.4	19.4
VEHICLES	-5.3	18.5

Strongest stock in group

	% change		Price
	4-week	52-week	
NEWMONT MINING	20.3	30.3	43
WEST POINT-PEPPERELL	14.5	93.2	57 1/4
BEVERLY ENTERPRISES	22.4	39.2	8 7/8
COLEMAN	57.7	95.0	68
INTERCO	16.0	91.1	3 5/8

Weakest stock in group

	% change		Price
	4-week	52-week	
FLEETWOOD ENTERPRISES	-12.2	34.2	26
CONSOLIDATED FREIGHTWAYS	-16.4	4.2	31 1/4
CROSS & TRECKER	-11.2	-20.2	12 7/8
INLAND STEEL	-8.1	34.9	44
CHRYSLER	-9.1	6.1	26 1/8

BRIDGE INFORMATION SYSTEMS INC.

MUTUAL FUNDS

LEADERS

4-week total return	%
GLOBAL GROWTH—JAPAN	8.0
PACIFIC GROWTH	5.8
AS GOLD SHARES & BULLION	5.3

Laggards

4-week total return	%
FMANN	50.0
PACIFIC GLOBAL CANADIAN	39.5
EMBIA SPECIAL	38.6

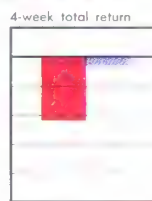
LEADERS

Four-week total return	%
STEADMAN OCEANOGRAPHIC TECHNOLOGY	-5.8
BRUCE	-5.1
DREYFUS CAPITAL VALUE	-4.8

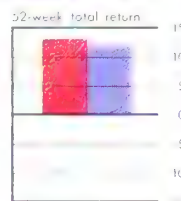
Laggards

52-week total return	%
STRATEGIC INVESTMENTS	-25.8
STEADMAN OCEANOGRAPHIC TECHNOLOGY	-21.8
UNITED SERVICES GOLD SHARES	-14.6

Relative Portfolios



Relative Portfolios



MORNINGSTAR INC.

RELATIVE PORTFOLIOS

Amounts invested at the present time of \$10,000 would grow to one year later	Foreign stocks	U. S. stocks	Money market fund	Treasury bonds	Gold
Investment figures indicate total returns	\$12,853 -0.75%	\$11,102 -2.41%	\$10,645 +0.16%	\$10,107 -1.00%	\$8,991 +0.91%

DATA RESOURCES INC.

Figures on this page are as of market close Wednesday, Mar. 1, 1989, unless otherwise indicated. Groups include S&P 500 companies only; performance and share prices are as of market close

Feb. 28. Mutual fund returns are as of Feb. 24. Relative portfolios are valued as of Feb. 28. A more detailed explanation of this page is available on request

THE FED SHOULD KEEP TIGHTENING—BUT GENTLY

The speedup in both producer and consumer prices in January is one more sign that inflation fears are justified and that restrictive monetary policy by the Federal Reserve Board is warranted to contain any further outbreak. The question is: How restrictive? Given the unique characteristics of the economic expansion, Fed policy is right on target.

The Fed's approach has been one of gradualism—an attempt to fine-tune the economy in a series of tightening moves based on perceived economic strength. The Fed wants to limit economic growth to a level that will not be inflationary in the long run—about 2.5% to 3%. In an economy nearing full utilization of both its labor force and its plant capacity, growth cannot exceed that range without putting upward pressure on inflation.

To be sure, inflationary pressures are developing in classic fashion. Strong demand from both domestic and foreign sources is beginning to overwhelm the supply of both products and labor. Stated more traditionally: There is too much money chasing too few goods and services.

However, the current business cycle differs greatly from the typical postwar model. First, the economy is coming off the greatest disinflation in half a century, a period that wrung inflationary expectations out of economic behavior. Prices will be slower to reaccelerate than they would be if expectations were already as high as they were in the 1970s. Second, as inflationary expectations build, financial deregulation assures that interest rates are freer to rise, thus choking down demand. And third, inflation is no longer determined by domestic pressures alone. With the globalization of the U.S. economy, worldwide production capacity and the international division of labor must be taken into account more and more.

This radically different structure of the economy makes it harder to find the appropriate degree of monetary restriction. A policy error on the tight side could tip the economy into a recession. But a series of incremental tightening moves allows the Fed to monitor the economy for signs that tighter policy is taking hold, thus reducing the chances of a slump. For now, the Fed should stay the course. When signs of past tightening finally show up, the financial markets will allow interest rates to fall, thus increasing the chances for the much-desired economic "soft landing."

STEP UP THE PACE OF LATIN DEBT WRITE-OFFS

Rioters hit the streets of Caracas in late February after Venezuela's new President, Carlos Andrés Pérez, boosted fuel and transportation prices to conserve cash to service his country's \$35 billion foreign debt. The riots are a stark reminder to international banks that

Latin America's crushing debt won't go away. With woes also threatening such fragile democracies as Brazil and Argentina, both of which are to hold presidential elections this year, banks are under pressure to help restructure Latin America's \$440 billion burden.

A shift toward easing the load, either through fast write-offs or reductions in interest rates, may already be in the wind. With Japan and other creditor nations advancing plans to aid Third World debtors, the Group of Seven industrial countries will meet in Washington at the end of March to review the debt strategy laid out in 1985 by then-Treasurer Secretary James A. Baker III.

Some international bankers concede that a change in tactics is already overdue. Many Latin American loans now days are made simply to keep earlier loans current. As a matter of fact, with many Latin loans now worth 30¢ on the dollar or less on the open market, a move to bring balance sheets in line with political and economic realities may be inescapable.

One way to speed debt reduction would be for the World Bank or the International Monetary Fund to guarantee bonds issued by debtors that would be worth less than existing loans. But it might not go far enough. Major U.S. banks have written off \$8 billion in Third World debt since 1987. It's time to step up the pace, lest increasingly unstable Latin debtors force even bigger write-offs on them.

THERE'S NO 'RIGHT' TO BEAR SEMIAUTOMATIC

When Patrick Purdy sprayed a schoolyard in Stockton, Calif., with gunfire on Jan. 17, killing and wounding 29, he horrified the nation. More than 30 cities around the country, including a dozen in California, have since imposed bans on semiautomatic weapons such as the one Purdy used that day. The notion is a valid one. But the only way the U.S. can minimize the likelihood of more Stocktons taking place will be to impose a national ban on the Russian-made AK-47, Israeli-made Uzi, and others of other semiautomatic guns.

Semiautomatic rifles were originally developed for the battlefield. They are useful for just two things: killing and maiming human beings. They are not, as the National Rifle Assn. contends, necessary or appropriate as sports weapons for hunting. They often wind up in the hands of dealers, gangs, and the kind of twisted individual who can fire on children in an unprotected schoolyard.

The NRA, with its effective lobbyists and zealous members, is bitterly fighting legislation in both chambers of the California legislature that would ban semiautomatics outright from the state. Gun dealers, who sold nearly 100,000 AK-47 Uzis, Chinese-made AKSS, and U.S.-made MAC-10s last year, worry that such a ban could produce a ripple effect nationwide. It should. Even with a California ban on semiautomatic rifles and pistols, they can be had for less than \$100 across the state line in Nevada. A federal law outlawing that kind of weapon could at least stop another Purdy from plunking down his money and taking more innocent lives.

March 20

RESULTS
100 COMPARE
PAGE 62

► THE TIME-WARNER DEAL ► EASTERN'S AGO

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BusinessWeek

MARCH 20, 1989

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THE MOMMY TRACK

BURLINGAME

MAR 13 1989

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Coping with
career and kids
in Corporate
America

PAGE 126

KATIE GLOCKNER

Part-time brand manager
Quaker Oats, Chicago,
with Thaddeus, age 2



12

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Fay Schroeder had a problem. She needed a quality office system for the loan operations area at First Commerce Corporation's lead bank in New Orleans. But aesthetics were going head to head with economics.

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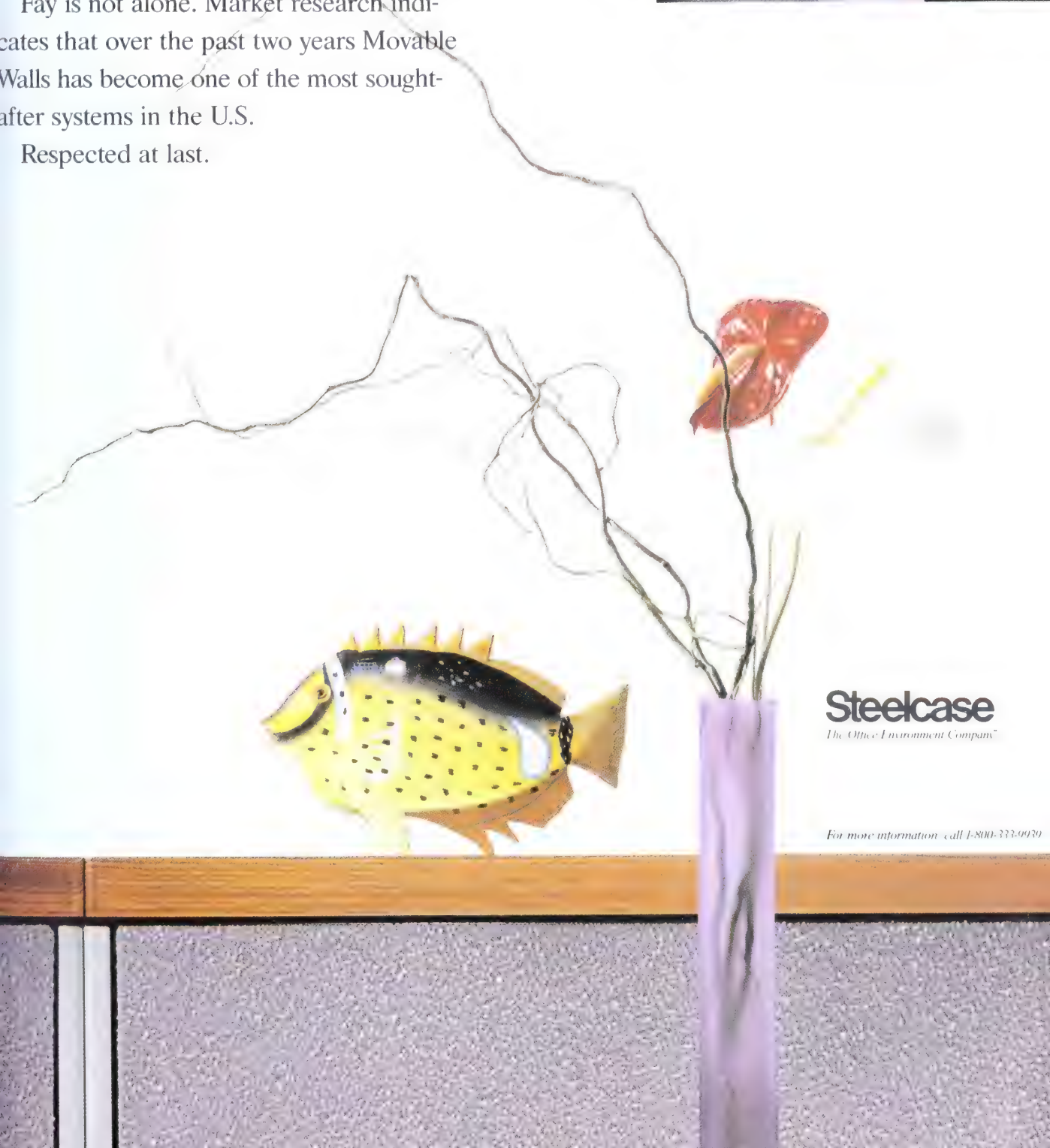
"Working with these options, I designed everything from data-entry to management-level workstations—without a big price tag.

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QUALITY TIME: CORNING GLASS ENGINEER BONNIE MILLIMAN WORKS ONLY TWO DAYS A WEEK SO SHE CAN CARE FOR HER DAUGHTERS

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Controversy is raging over a mother's place in the corporation. Must women opt for a slow track to spend more time with their children? A number of corporations are answering no and accommodating mostly upper-level executives with flexible hours, part-time work, and extended leaves. But should this new flexibility be available to all or to a chosen few?

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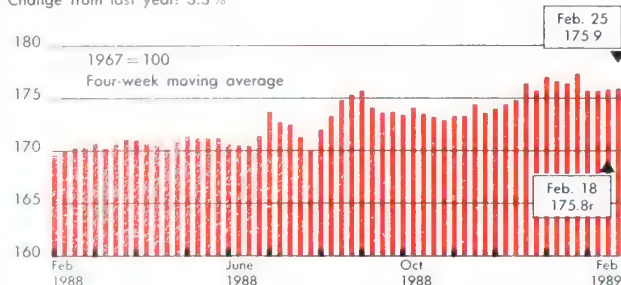
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One labor law, not two
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BusinessWeek Index

PRODUCTION

Change from last week: 0.1%
Change from last year: 3.3%

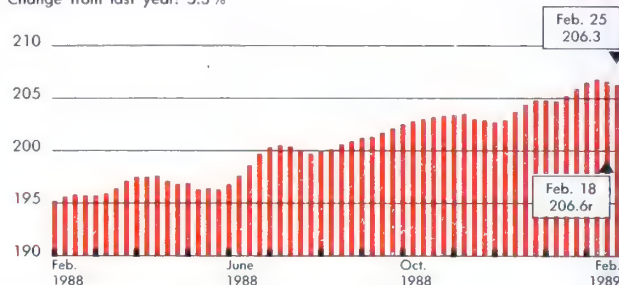


The production index increased slightly for the week ended Feb. 25. The seasonally adjusted output of lumber, electric power, and paperboard rose. Production levels of autos, steel, coal, rail-freight traffic, crude-oil refining, and trucks were down. Paper output was unchanged for the week. Prior to calculation of the four-week moving average, the index dropped to 176.7 from 176.9. In February the index declined to 175.9, from 177.3 in January.

BW production index copyright 1989 by McGraw-Hill Inc

LEADING

Change from last week: -0.1%
Change from last year: 5.3%



The leading index fell for the week ended Feb. 25. Lower stock prices, higher bond yields, and a slower pace in real estate loans contributed to the decline, offsetting faster growth in M2. Growth in materials prices was unchanged, and data on business failures were unavailable for the week. Before calculation of the four-week moving average, the index declined to 206.1, from the previous week's 206.5 level. The February index stood at 206.3, up from January's 205.9.

Leading index copyright 1989 by Center for International Business Cycle Research

PRODUCTION INDICATORS

	Latest week	Week ago	% Change year ago
STEEL (3/4) thous. of net tons	1,956	1,972 #	-1.0
AUTOS (3/4) units	149,660	146,691r #	17.0
TRUCKS (3/4) units	90,831	93,667r #	7.7
ELECTRIC POWER (3/4) millions of kilowatt-hours	54,857	55,761 #	8.9
CRUDE-OIL REFINING (3/4) thous. of bbl./day	12,675	12,699 #	-1.0
COAL (2/25) thous. of net tons	19,398 #	19,351	-0.6
PAPERBOARD (2/25) thous. of tons	747.7 #	743.7r	0.1
PAPER (2/25) thous. of tons	746.0 #	745.0r	-2.9
LUMBER (2/25) millions of ft.	487.3 #	454.9	-8.4
RAIL FREIGHT (2/25) billions of ton-miles	18.9 #	19.6	-2.1

Sources: American Iron & Steel Inst., Ward's Automotive Reports, Edison Electric Inst., American Petroleum Inst., Energy Dept., American Paper Inst., WWPA, SFPA, Association of American Railroads.

FOREIGN EXCHANGE

	Latest week	Week ago	Year ago
JAPANESE YEN (3/8)	129	128	128
GERMAN MARK (3/8)	1.86	1.84	1.67
BRITISH POUND (3/8)	1.72	1.72	1.84
FRENCH FRANC (3/8)	6.32	6.25	5.66
CANADIAN DOLLAR (3/8)	1.20	1.20	1.25
SWISS FRANC (3/8)	1.59	1.57	1.38
MEXICAN PESO (3/8) ³	2,362	2,353	2,300

Sources: Major New York banks. Currencies expressed in units per U. S. dollar, except for British pound expressed in dollars.

PRICES

	Latest week	Week ago	% Change year ago
GOLD (3/8) \$/troy oz	394.600	384.050	-9.6
STEEL SCRAP (3/7) # 1 heavy, \$/ton	123.00	123.00	3.4
FOODSTUFFS (3/6) index, 1967=100	231.4	232.4	7.0
COPPER (3/4) ¢/lb.	148.7	144.8	46.5
ALUMINUM (3/4) ¢/lb.	102.5	102.0	-1.7
WHEAT (3/4) # 2 hard, \$/bu.	4.47	4.40	42.4
COTTON (3/4) strict low middling 1-1/16 in., ¢/lb.	55.73	55.35	-6.2

Sources: London Wed. final setting, Chicago mkt., Commodity Research Bureau, Metals Week, Kansas City mkt., Memphis mkt.

Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment
1 = Western Wood Products Assn. 2 = Southern Forest Products Assn. 3 = Free market value NA = Not available r = revised NM = Not meaningful

LEADING INDICATORS

	Latest week	Week ago	% Change year ago
STOCK PRICES (3/3) S&P 500	288.98	291.52	8.1
CORPORATE BOND YIELD, Aaa (3/3)	9.75%	9.70%	5.1
INDUSTRIAL MATERIALS PRICES (3/3)	103.8	102.6	6.1
BUSINESS FAILURES (2/24)	NA	NA	NA
REAL ESTATE LOANS (2/22) billions	\$312.8	\$312.7	13.1
MONEY SUPPLY, M2 (2/20) billions	\$3,094.2	\$3,083.8r	4.1
INITIAL CLAIMS, UNEMPLOYMENT (2/18) thous.	317	326	-3.1

Sources: Standard & Poor's, Moody's, Journal of Commerce (index: 1980=100), Dun & Bradstreet (failures of large companies), Federal Reserve Board, Labor Dept. CIBCR seasonally adjusts data on business failures and real estate loans.

MONTHLY ECONOMIC INDICATORS

	Latest month	Month ago	% Change year ago
BUSINESS WEEK PRODUCTION INDEX (Feb.)	175.9	177.3r	3.1
BUSINESS WEEK LEADING INDEX (Feb.)	206.3	205.9r	5.1
MANUFACTURERS' INVENTORIES (Jan.) billions	\$357.3	\$354.2	7.1
12 LEADING INDICATORS COMPOSITE (Jan.) index	145.7	144.9r	5.0

Sources: BW, CIBCR, Commerce Dept.

MONETARY INDICATORS

	Latest week	Week ago	% Change year ago
MONEY SUPPLY, M1 (2/20)	\$789.5	\$784.3r	3.1
BANKS' BUSINESS LOANS (2/22)	310.0	311.0	5.1
FREE RESERVES (2/22)	593r	1,071r	-33.1
NONFINANCIAL COMMERCIAL PAPER (2/22)	107.9	108.2	28.1

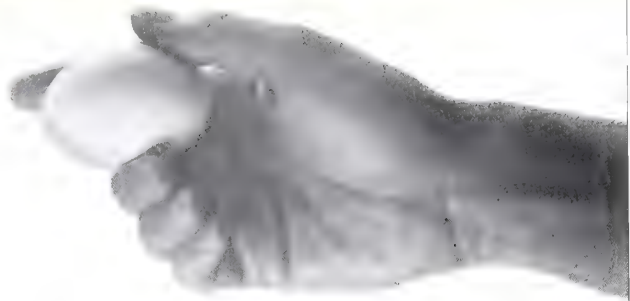
Sources: Federal Reserve Board (in billions, except for free reserves, which are expressed for a two-week period in millions).

MONEY MARKET RATES

	Latest week	Week ago	Year ago
FEDERAL FUNDS (3/7)	9.59%	9.87%	6.51%
PRIME (3/8)	11.50	11.50	8.50
COMMERCIAL PAPER 3-MONTH (3/8)	9.80	9.86	6.56
CERTIFICATES OF DEPOSIT 3-MONTH (3/8)	9.95	10.00	6.61
EURODOLLAR 3-MONTH (3/1)	10.03	9.68	6.71

Sources: Federal Reserve Board, First Boston

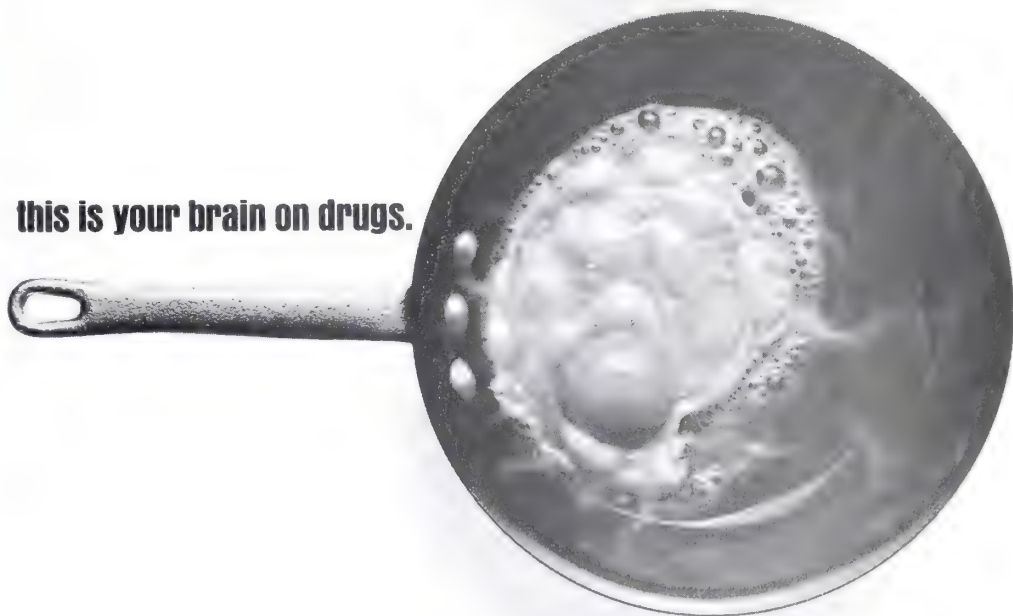
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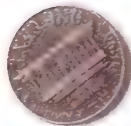
For 61 cents a day, here's what GTE's new



You'll have the satisfaction of getting more features—there are 13 in GTE's CentraNet 1000 package—at less cost than ever before.



You'll have an advanced, highly efficient business communications system, without having switching equipment on your premises.



Each month, you'll be able to check how much each station's phone calls cost you.



Thanks to individual station billing, you'll be able to ask the new employee about all those calls to New York—at your expense.



24 hours a day, 365 days a year, GTE's computerized, self-diagnostic systems will work to keep things running smoothly.



If something should go wrong, the chances are we'll have it fixed before you even notice it.



You'll be able to tell by the sound of the ring whether a call is coming from across the hall or across the country.



You'll have a business phone system that can grow with you: GTE's CentraNet 2000 and 3000 packages offer even more sophisticated features.



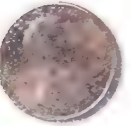
Your communications will have the quality you'd expect from GTE's advanced network.



GTE's CentraNet service means that you'll be able to schedule changes months in advance, or as soon as this morning.



If the lights should go out, your telephone service will stay on.



When Burt in Bakersfield won't get off the phone, that important call from Encino will go automatically to your secretary.



Your speed dialing feature will remember the eight numbers you call most often.



You may be able to beat someone to the best table at Mario's, because you only have to punch in two numbers, not the usual seven.



GTE's CentraNet service will turn the ordinary touchtone phones you already own into highly sophisticated business tools.



Your small branch offices will be able to have the same telephone features as your big home office.



You may be able to breathe new life into your aging key system, without having to buy yet more expensive equipment.



If Deborah needs a phone that has more features, you'll be able to give it to her without having to give the same features to John, Linda, Michael and Melissa.



You'll be able to add lines by making one phone call to a GTE Account Executive.



You'll be able to delete lines by making one phone call to a GTE Account Executive.



You'll probably pay less for your fire and theft insurance, since you won't have to invest in costly switching equipment to insure.



You may be able to catch Doug before he leaves for lunch, because like everyone else, he'll have his own direct line.



If you land a big contract, CentraNet will offer more than congratulations: our optional features range from 8-party conferencing to automatic call distribution.



You'll be able to answer the phone in your partner's office without even leaving your car.

CentraNet[®] can do for your business phone.



You'll see a lot less of your phone repairer, since the switching equipment is monitored and maintained on GTE's premises, not yours.



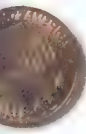
You'll probably be able to tear up that oh-so-expensive service contract.



You'll have an extra office or storeroom, instead of a room that's packed full of telecommunications equipment.



You'll be able to impress your business associates with "Excuse me, I have another call on this line." (They'll be even *more* impressed if they happen to be the other call.)



Your company can expect to save a bundle in trunk charges. There aren't any.



Your switching equipment isn't going to need air conditioning in summer (remember, you don't have any switching equipment).



Your switching equipment isn't going to need heating in winter (ditto).



CentraNet can save a business with 160 lines \$51,450 in five years, compared to a PBX system. (Ask your GTE Account Executive to explain the assumptions behind these numbers.)



You'll be able to transfer calls without needing a master's degree in telecommunications.



You'll have the most advanced business phone system of 1989. And 1990, 1991, 1992... the point is, as soon as we get new technology, so do you.



You'll only need to hit four numbers, to find out what's going on in the Sacramento office.



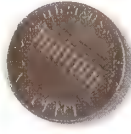
Thanks to direct inward dialing, every call doesn't have to go through your receptionist. So there'll be more time to help your customers who really need it.



If you're an accountant, you'll be able to cope with the usual overload in April, without having spare capacity in September.



Same for ski operators after the first snowfall, fireworks manufacturers on the Fourth, florists' shops on Valentine's Day.



You can change your mind about the features you need, and not have to change \$20,000 worth of equipment.



Installation won't mean weeks of hassle and headaches. If the wiring's already in place, all it often takes is a phone call.



With CentraNet's station hunting feature, incoming calls can be automatically routed to ring phones that aren't busy.



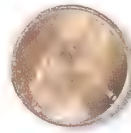
You can find out who in your company uses which features, when and how often.



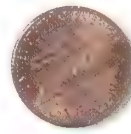
You'll be able to invest the capital you don't spend on phone equipment on something else that your business really needs.



You'll be able to brainstorm with Jack (in Detroit) and Jacqueline (in Delaware) simultaneously, thanks to 3-way conferencing.



When you're talking to Ed, and Bill calls, you can answer him, buzz Brian, tell Bill what Brian said, then get back to Ed.



You'll sound like a million dollar corporation, even if you're just a two-person company.



We could go on, but it might be better to call 1-800-325-6844, and speak to a GTE Account Executive. Just say you'd like their two cents' worth on what CentraNet can do for you.



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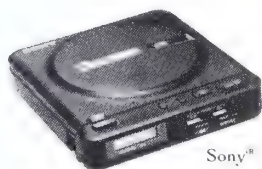
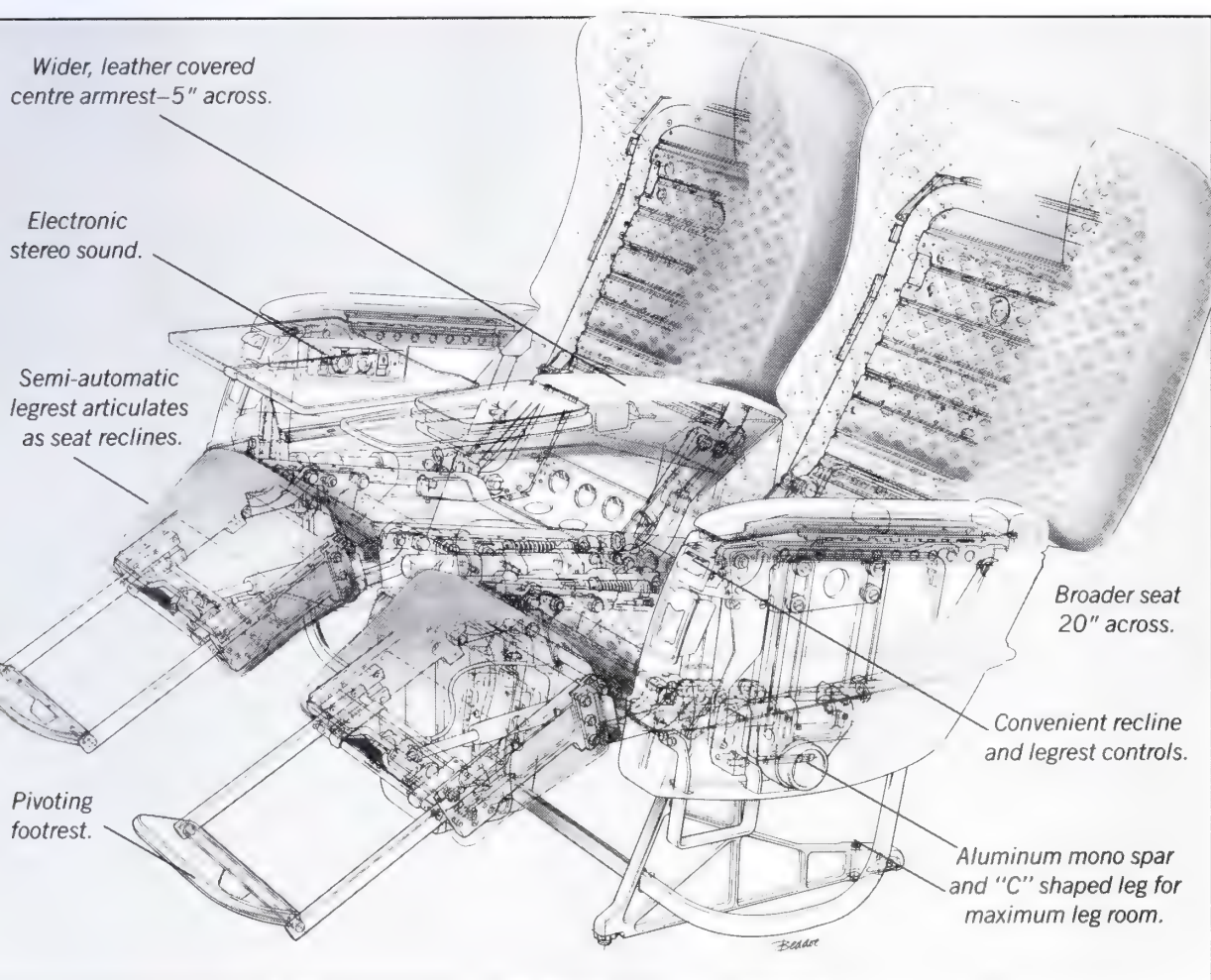
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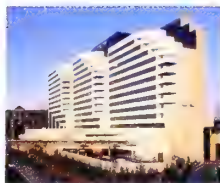
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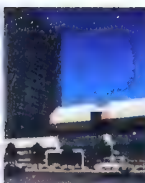
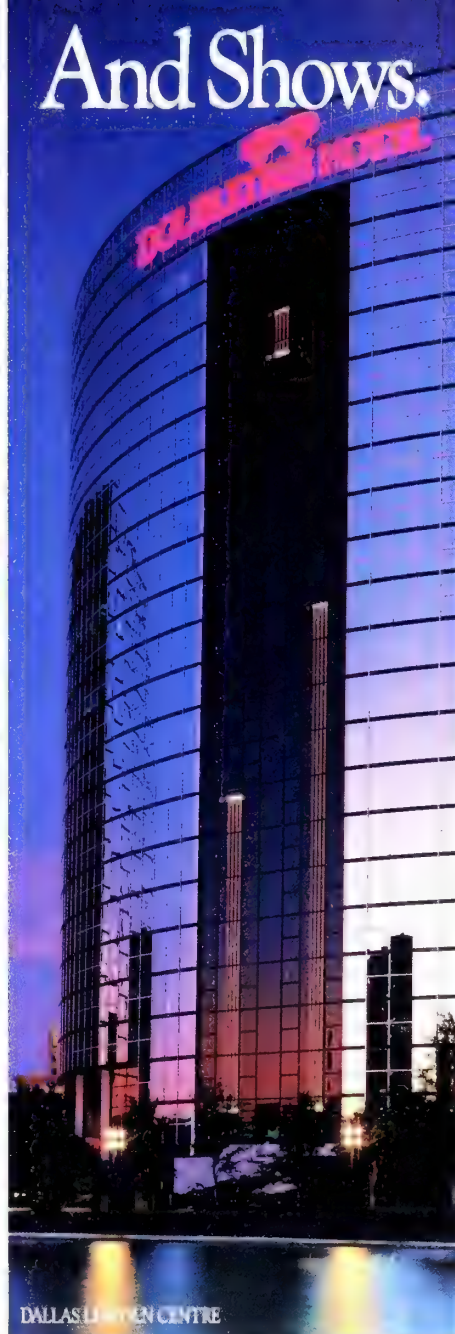


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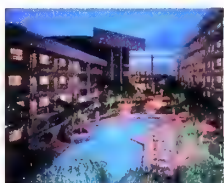
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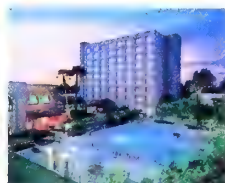
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DEREGULATION REQUIRES A FIRM HAND ON THE REINS

Regarding "Why Bush's S&L bailout is fundamentally flawed" (Economic Viewpoint, Feb. 27): As a horseman of modest talents, I want to thank your staff and Robert Kuttner for invoking an image of deregulation that is as hilarious as it is sobering [the statue, outside the Federal Trade Commission building, of a man reining in a wild horse]. Eliminating interest rate ceilings for deposits when we did not have in place the wherewithal to police the quality of lending and had entered a period of severe monetary restraint represents the kind of high roll by which we won a skirmish but may have lost another battle against inflation.

Mr. Kuttner's readable and succinct analysis of the S&L problem addresses cause and effect relationships bearing upon all our deregulation experiments. The time has come to franchise and take public a nationwide chain of riding academies to teach rough-riding folk everywhere something about the fine art of economic horsemanship.

Otto F. Grote, President
 Derby Securities Inc.
 New York

WHY GENERAL DYNAMICS WANTS TO FLY WITH JAPAN

In response to "A deal we should knock out of the sky" (Editorials, Feb. 20), I would like to make several points:

First, the basic policy decision to pursue the FSX program was made by the U.S. government based on diplomatic, defense, technology, trade, and policy issues. General Dynamics Corp. and other U.S. companies are participating in this program as instruments of the U.S. government and this decision.

Second, our company will not "turn over all its technology on the F-16." The subject of technology transfer received a great deal of scrutiny by both the State Dept. and the Defense Dept. very early in the program. Very strict guidelines were established as to what technology was releasable to Japan and, most important, what technology we should re-

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ceive from Japan as a result of this program. This is truly a "two-way-street" technology transfer program.

Finally, let's consider what "calling a halt," as BUSINESS WEEK demands, would really mean. You are entirely correct when you state: "If Japan wishes to build a fighter of its own by the late 1990s, it's free to do so." They can and they will. As a result, the Japanese probably would continue on their plan to establish an aerospace industry and would become an international competitor. What would really be "shortsighted," to take another line from your editorial, is to take the U.S. out of play in the naive belief that we are the only game in town, or that somehow the Japanese won't be able to pull it off without our help. If we halt this program at this time, we have opened the way for a future international aerospace industry competitor without any ties to the U.S. government or U.S. industry. That is the route taken by some industries in the last couple of decades, and everyone knows where that head-in-the-sand attitude got us.

Herbert F. Rogers, President
 General Dynamics Corp.
 St. Louis

IS BUSINESS FIDDLING WHILE THE EARTH BURNS?

It was disheartening to read "When the rivers go dry and the ice caps melt..." (Science & Technology, Feb. 13) and see the response of U.S. business to global warming. Instead of fo-

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"Management must guide the forces of change..."

— John W. Teets, Chairman



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The Greyhound Corporation has been recast. From the crucible of change has emerged a new Greyhound, tempered for strength and reshaped for the future.

The job of management always has been to see the company not as it is, but as it can grow to be. The new Greyhound is the result of this vision, built through a five-year restructuring program.

Hard choices were faced; tough decisions were made. Subsidiaries with annual sales of \$3 billion,

including the company's nationwide bus line, were divested. At the same time, new businesses with excellent growth and profit potential were established or acquired.

For example, Purex household and laundry products were added to the personal care and packaged foods brands of Greyhound's Dial Corporation. Premier Cruise Lines, the official cruise line of Walt Disney World, was launched. Dobbs food service for air



Travelers was acquired, complementing Greyhound's existing airport and food service businesses. General Motors' RTS transit bus manufacturing and parts operation was purchased to expand Greyhound's top-ranked intercity coach-building business.

Today, Greyhound's four business segments — consumer products, services, transportation manufacturing and financial — produce revenues at a \$3 billion annual rate.

With the restructuring of Greyhound's core businesses completed, management is concentrating on further improvement of operating returns. Change is inevitable, and management must guide the forces of change to create value for shareholders.

At Greyhound, we believe in renewing the company day by day.

The Greyhound Corporation



Readers Report

cusing on how the warming could be slowed or stopped, the focus continues to be on accepting this calamity while continuing to profit. If the whole world thinks this way, Homo sapiens may be writing its last chapter in the history books.

Bob Phillips
Annandale, Va.

CARPAL TUNNEL SYNDROME: ATTACK CAUSES, NOT SYMPTOMS

As a physical therapist with many years' experience with industry in general and with carpal tunnel syndrome (CTS) in specific, I feel there were several points that you failed to make in "An invisible workplace hazard gets harder to ignore" (Labor, Jan. 30).

Your work clearly identifies the extraordinary problems and costs associated with CTS and other cumulative trauma disorders. However, what business and industry need to know is that there are solutions for the vast majority of incidents and there is more known about the causes than is reflected by your article. For instance, five particular motions performed on a repetitive basis are a primary cause of CTS. When workers are educated about the five motions and helped to adjust their work situations to a more ergonomically sound condition, most cases can be relieved or even eliminated. In short, prevention education combined with medical-ergonomic job analysis can save industry millions of dollars.

As you mention, surgery can ease pressure on the median nerve. But this deals with the symptoms and not the causes. In our experience, people who have had surgery are often candidates for multiple surgeries due to nonrelief of symptoms or return of symptoms. This occurs because the individual was not given the tools to truly eliminate or minimize the cause of their problem.

Another common fallacy lies in using splints much as you illustrated, as well as other elasticized models. While they help to keep the wrist straight, the median nerve is still compressed by the tight-fitting nature of the splint. The end result is that most of the positive effect of wrist immobilization is offset by the negative effects of wrist constriction.

Glenda L. Key
President
Key Functional Assessments Inc.
Minneapolis

Your article about repetitive motion injuries calls attention to a prevalent medical problem. I was disappointed, however, to find that it described CTS as the result of repetitive motion. Certainly many individuals who have this

condition will have increased symptoms with many forms of hand activity, vocational or avocational. But your statement that frequent bending of the wrist causes tendons or tissue to swell and pinch the median nerve is only theory. There is no generally accepted scientific basis by which the nerve abnormality underlying CTS can be demonstrated to be the result of hand activity.

In view of the record fines placed on employers, the economic impact to society, and the suffering individuals with this condition, we must search for the cause of these problems in scientific fact rather than in casual associations and clinical rumors.

Dr. Peter A. Nathan
Director
Portland Hand Surgery &
Rehabilitation Center
Portland, Ore.

ECONOMICS EXPLAINS IT ALL FOR YOU

Regarding "Is the deficit too high? Yes. Should it be higher? Maybe" (Economic Viewpoint, Feb. 20): Economics is a fascinating subject! I had no idea I bought a Japanese VCR because the Reagan Administration sold bonds to Japan. And now I learn the thing won't even produce any income. If only I had known, I would have tried to buy a domestic income-producing model—but, wait, I forgot about those darned bonds. Fascinating.

H. C. Edgecombe Jr.
Pass Christian, Miss.

HOW TO KEEP IN TOUCH WITH E-MAIL'S FUTURE

By focusing on the planned interconnection of domestic public electronic mail networks, your recent article "Electronic mail: Neither rain, nor sleet, nor software..." (Top of the News, Feb. 20) overlooked several areas far more likely to influence the growth of the E-mail industry.

I refer to the interconnection of dissimilar private message systems within an organization, the interconnection of private message networks to public message services, and the international agreements for linking public E-mail networks in the U.S. to those operated in many countries abroad. All of these developments are made possible by widespread deployment of the X.400 telecommunications standard, which permits E-mail communications between dissimilar computer systems.

Clearly, the ability to communicate between Telenet's Telemail, British Telecommunications' Dialcom, AT&T Mail,

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Readers Report

MCI Mail, and Western Union's Easylink is important. But business customers are also interested in establishing corporate-wide messaging networks, linking these networks to public message services, and communicating domestically and overseas with companies operating dissimilar computer systems. Most new revenue in the industry will derive from these X.400 private-to-public system links, not from traffic between public E-mail vendors.

For the record, Telenet has more private-to-public and public-to-public X.400 interconnections than any other E-mail system vendor. Also, the MCI/CompuServe interconnection referred to in your article uses a proprietary protocol, not the international X.400 standard.

Stuart L. Mathison
Vice-President
Telenet Communications Co.
Reston, Va.

I would like to correct the analysts' evaluation of the McDonnell Douglas OnTyme mail service as a "money-losing" operation. OnTyme has been profitable for many years. In fact, these profits fuel our major electronic messaging R&D projects and enable us to introduce services, such as the upcoming "PC OnTyme Plus," that offer extended features at reduced rates.

As your story indicates, tremendous payback awaits E-mail vendors who make the service as easy to use as the telephone. The technology is a foundation for a diverse range of communication possibilities. This is why we are fully committed to providing services that span electronic messaging from basic E-mail to full-function electronic data interchange, all with X.400 compliance.

Jeremy J. Causley
President
McDonnell Douglas Information
Systems Co.
Irvine, Calif.

A RESPONSE FROM KIDDER PEABODY

Regarding "The body count keeps growing at Kidder Peabody" (Finance, Feb. 20): There are many errors of fact and countless levels of innuendo, but I would like to address the most egregious:

■ Kidder, Peabody Group Inc. is characterized as being in a "meltdown." The facts are that we have lost less than 1% of our 6,200 people and a very small percentage of our investment banking talent. Those that have left will be replaced, and we are moving ahead.

■ General Electric Co. isn't going to sell the retail and institutional brokerage

business. This has been denied time and time again, by me and by GE. These are critical legs of our business, and it would be foolish to spin them off.

■ The investment banking operations are not going to be merged into GECC. They are two totally separate entities. Apples and oranges. To flatly state that this would happen reflects a naive understanding of our business.

■ Your numbers concerning the investment banking of the 1988 bonus pool are wrong. As a group, investment banking received a higher percentage of pretax, prebonus income than it did for 1987.

■ Investment banking is not going to be cut in half, and compensation is not going to be brought "more in line with GE Capital pay scales." This again reflects an incredibly naive understanding of the two businesses. We are going to pay competitive market rates to attract the highest quality bankers.

Michael A. Carpenter
President and CEO
Kidder, Peabody Group Inc.
New York

INSIDE THE U.S. EMBASSY IN BEIJING

Your commentary "The U.S. in China: Letting a new caution bloom" (International Business, Jan. 30) contains totally inaccurate and misleading references. I would like to correct this irresponsible reporting.

There was no "stunned" group of American diplomats who heard me warn that China's reform program "might be verging on 'retrogression,'" nor have I said that "a full reevaluation of U.S.-China relations might be necessary" (your correspondent's quotes).

I have no idea what meeting she was referring to nor what the source of these spurious quotations might have been. As any ambassador would, I have called on my staff to continue analyzing and reporting fully and candidly on economic trends here and their significance.

Winston Lord
Ambassador
U. S. Embassy
Beijing

Editor's note: Ambassador Lord's remarks were reported to us by State Dept. employees who attended a three-day meeting at the U. S. embassy in Beijing, from Nov. 28 through Dec. 1, for senior staff only.

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MORE LIKE US: MAKING AMERICA GREAT AGAIN

By James Fallows

Houghton Mifflin • 245pp • \$18.95

THE U.S. ISN'T JAPAN— AND IT SHOULDN'T TRY TO BE

Three years ago, Washington journalist James Fallows packed up his wife and two sons and moved to Tokyo. From that decision came a memorable series of columns on Japanese life etched with humor and wit. In a personal, mischievous style, Fallows has poked gently at the inflated Japanese psyche, shattered some myths about the Asian powerhouse, and picked gently at the scab of racism.

This time we get to win, but only after going through a dark struggle with self-doubt and renewing our faith in what Fallows regards as our most valuable strength, our individualism.

There's nothing wrong with this message. Television evangelists and senators get away with worse every day, and nobody understood its inspirational appeal to Americans better than Ronald Reagan. It's also an honest expatriate

reaction. America does look big and rich and boundless from overseas. But after you say that, what else? Fallows doesn't know what makes us tick any more than you or I, but he devotes a large part of this book to pretending that he does. Many pages are spent on Fallows' personal experience of America, starting with his boyhood in Redlands, Calif. He rummages through a card catalog of academic theories about making America great again and drags us through an irrelevant, oily confession about how, as a Harvard student, he starved his way out of the Vietnam draft. Reading the last

gave me the same crawling sensation as listening to John Tower take the pledge.

All of this is too bad, because when the material is fresh, Fallows can be incisive. There are trenchant parts in this book, but you have to search for them. Here's Fallows on Japan's dedication to racial homogeneity: "The let's-all-be-the-same ethic is Japan's greatest vulnerability. Already the country is trying to figure out how to cope with the 'returnees,' the Japanese children who have grown up in New Jersey or London while their fathers did battle for Matsu-shita or Nissan. When the children come back, they're no longer quite Japanese."

And on Japan's treasured insularity: "The United States is the closest approximation to a friend that Japan has. Whenever waves of anti-Americanism



If you read his column in *The Atlantic* and other publications, you probably haven't forgotten the day Fallows and his sons visited the neighborhood public bath. "We spent half an hour in the requisite scrubbing and cleansing rituals before entering the bath itself. Even so, all the Japanese men stepped out the instant our skin touched the water. We were not really that dirty."

As Fallows kept up a streak of winning stories on Japan's work ethic, its hidden poor, and its robotized classrooms, I began sending copies to friends. Then something must have gone wrong. Fallows decided to write a book—but not about his personal experiences in Japan. *More Like Us*, as the title implies, is about the U.S., or more specifically, about the U.S. vs. Japan.

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started breaking over me in Korea, China, or the Philippines, I'd wait until the subject switched to Japan and sit back to hear some real vitriol."

Turning from that to the debate about whether the U.S. is losing the economic race with Japan is like switching from live theater to the family hour. Fallows reminds us that many Japanese believe that the U.S. has already lost. "America's problems derive, in the Japanese view, from too many vacations, too much greed, too little discipline—and, as only a few actually say but many seem to believe, too few Asians and too many blacks." Fallows doesn't know whether to feel grateful or insulted when a Japanese friend tells him: "I still think America can come back."

Fallows, of course, believes it can. But he concedes there are days when even he has doubts. Where he breaks company with the decline-of-America crowd is over remedies that would make us more like Japan, such as consensus management, school tracking, and picking the industries of the future. What works for Japan's closed, self-sacrificing society would destroy America just as surely as our free-spending individualism would ruin Japan, he believes.

Unfortunately, Fallows has trouble prescribing what we should do. That's partly because the strengths he values most in the U.S.—our adaptability, our mobility, and our diversity—are by definition unmanageable. Secretary of Disorder, anyone? Generally, he favors fewer restrictions. He wants more immigration and easier standards for doctors, lawyers, accountants, teachers, and other professionals. He's also for deemphasizing IQ and other standardized tests, especially the SAT, to create more opportunity for poor and culturally disadvantaged kids to attend college and move into the professions.

But how these changes might help remedy such American dilemmas as drug abuse, illiteracy, or a frightening high-school dropout rate isn't part of this book. Japan's tightly regulated culture simply doesn't have such problems, and you wonder if Fallows thinks they are a price we pay for an open society.

More broadly, Fallows never develops the argument that seems most crucial to his thesis: that this country lacks strong national leadership. Americans will sacrifice enormous energies for the right cause, he believes. The problem is that it usually takes a popular war or a Sputnik to unleash those passions, and no recent President had such an opportunity. Wistfully, Fallows suggests that a new shock to the nation's confidence, equivalent in magnitude to a "nonviolent Pearl Harbor," might serve as a rallying point.

Unfortunately, economic competition seldom provides such a clear signal, he notes.

Ten chapters by a facile writer are not too much to read, and you can easily skip the slow parts. But if you're a Fallows fan, prepare to be disappointed.

BY ROBERT J. DOWLING

Dowling is BW's senior editor for international coverage.

BOOK BRIEFS

STRANGE GROUND: AMERICANS IN VIETNAM 1945-1975

By Harry Maurer
Henry Holt • 634pp • \$29.95

You have to like Harry Maurer's honesty. Before introducing us to Vietnam veterans in this rich oral history, the author of *Strange Ground* writes: "I am a draft dodger." Describing his antiwar undergraduate days and his guilt over snagging a deferment while others died in the jungles, Maurer, BUSINESS WEEK's deputy chief copy editor, makes himself the book's central character. He represents the millions of draft-age men who didn't put on a uniform, the ones who have wondered ever since: What was it like?

Strange Ground captures the harsh reality of being there—hollow-bellied fear, everyday brutality, numbing boredom, drugs, and death. It also describes an intimacy that those who have never been shot at cannot understand, what Maurer calls the mutual "respect and trust" that prevailed during combat and whose absence left many a vet feeling empty back in civilian life.

But Maurer doesn't stop with the grunts. To chronicle 30 years of American involvement, he taped the bitter reminiscences of eager bureaucrats who served in Vietnam and who tried—but failed miserably—to win hearts and minds. He also sought out blunt-spoken retired officers. Among them is one whose voice was sadly ignored at the time: John H. Cushman, who eventually retired as an Army lieutenant general. Cushman's idea: Let South Vietnamese troops police their own countryside, while U.S. soldiers cut the vital Ho Chi Minh Trail supply line.

Those looking for clear-cut lessons about how to avoid another Vietnam-like nightmare won't find them in *Strange Ground*. This very human book should be read for what it is: a wrenching compendium of memories. As one old infantryman puts it: "The past is a sickness you can't cure."

BY DAVE GRIFFITHS

Griffiths was with the 11th Armored Cavalry Regiment in Vietnam in 1970 and 1971.

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BY GENE KORETZ

WILL THE NEW LEADING INDICATORS BE AS MISLEADING AS THE OLD?

The government's newly revised index of leading indicators is promoted as a more accurate gauge of the economy's direction. And at least over the past year or so that appears to be true, since the new index would have turned in a far stronger performance than the old—a finding that appears in line with the still-healthy pace of business activity.

Whether the new leading index will prove more reliable when it signals a slowdown or recession is another question, however. The old index declined for three consecutive months in mid-1984, for example, flashing the time-honored signal of a pending recession that never occurred. "Unfortunately," says economist Michael Evans of Evans Economics Inc., "the new index is actually far worse, since it would have declined for seven consecutive months in 1984."

Similarly, although it didn't decline for three straight months in late 1987, the old index did drop a disconcerting 0.8% from September to November, raising fears of another coming downturn—which also failed to occur. Yet it turns out that the presumably more reliable revised index would have declined for five consecutive months from September through January, 1988.

In sum, concludes Evans, "whereas the old discredited index gave two ambiguous signals of recession where none occurred, the revised index removes these gray areas and unmistakably identifies two recessions that never materialized." As a result, "the new index is no better than its predecessor, which means that it provides no guidance whatsoever about where the economy may be heading."

RIISING RATES MAY FINALLY CURB THE URGE TO SPLURGE

Will the 350-basis-point rise in short-term interest rates over the past year act as a significant brake on consumer spending in the months ahead? Economist Bruce Steinberg of Merrill Lynch & Co. points to the growing number of homeowners with adjustable-rate mortgages (ARMs) as a key reason why the answer is probably yes.

Steinberg calculates that 8 million to 9 million households now hold adjustable-rate mortgages, worth about \$500 bil-

lion—around 25% of total home-mortgage debt. Virtually all these households will experience rate hikes this year, but the biggest increases will be felt by the 70% whose ARMs are linked to one-year Treasuries or other market interest rates that have risen sharply in the past year. Even with a two-percentage-point annual cap on adjustable-rate increases, such households are likely to face mortgage payment hikes averaging about \$150 a month this year, he says.

As for the offsetting effect of higher interest income, Steinberg concedes that households with adjustable-rate mortgages tend to have incomes well above the national average. However, he notes that an overwhelming 83% of ARM holders have interest-rate-sensitive assets worth less than 25% of their mortgage debt. Says Steinberg: "Such households, generally baby boomers in midlife, will get little relief from higher interest income as their cash flow is squeezed by rising mortgage payments."

Not everyone agrees that this will restrain consumption significantly. Economists at First Boston Corp., for example, observe that even if the total cost of a two-percentage-point increase in ARMs payments were subtracted from consumer spending, the impact would be just \$10 billion to \$15 billion, compared with a \$214 billion rise in personal consumption expenditures last year. And that's not counting the offsetting effects of higher mortgage-interest tax deductions.

Steinberg thinks the impact at the margin could be considerable, however. "You have to factor in the other \$400 million in adjustable-rate nonmortgage consumer debt," he says, "as well as the negative effect of higher interest rates on household wealth and on consumers' willingness to take on new debt."

A TAX SURPRISE TAKES A BITE OUT OF THE DEFICIT

The federal budget picture continues to brighten, reports economist William V. Sullivan Jr. of Dean Witter Reynolds Inc. Paced by a 14.8% rise in the corporate tax take and an 8.3% increase in personal income tax receipts, tax collections in the first third of fiscal 1989 are running 8.6% over 1988, compared with Administration projections of only 7.3% for the full fiscal year.

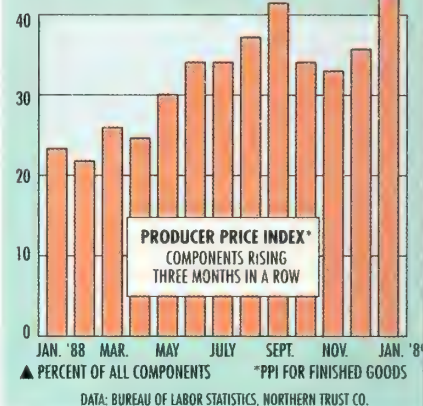
Meanwhile, despite rising interest expenses and outlays sparked by the thrift crisis, total spending is actually falling behind projections. The bottom line: a 2.3% decline in the unified deficit so far in fiscal 1989.

JANUARY'S PRICE SURGE SEEMS MORE THAN A FLASH IN THE PAN

January was the cruelest month for inflation-watchers, as the produce price index, up 1%, and the consumer price index, up 0.6%, posted their largest increases in several years. But though the news rocked the financial markets many economists remain unperturbed. In their view, the underlying inflation rate still is moving along at a 4%-to-5% rate, and the January numbers are largely a fluke reflecting faulty seasonal adjustment and the coincidental confluence of a number of individual price hikes (page 22). As the economy slows price pressures inevitably will ease.

This reassuring scenario may indeed unfold as the year progresses, but economists Robert F. Dieli and Robert G. Dederick of Chicago's Northern Trust Co. think the evidence points the other

PRICE INCREASES ARE GROWING MORE PERSVASIVE



way. To prove the point, they have constructed a monthly "diffusion index" of producer prices. The index measures the percent of total components in the PPI that have moved higher for three consecutive months. "We chose a three-month span," they say, "in order to filter out erratic price movements and focus on continuing price pressures."

The diffusion measure tells a dramatic story. Since late 1987, the percent of the PPI's components posting three-month increases has risen steadily from 20% to a high of 42% (chart). "More prices are rising, and in the aggregate, they are rising more quickly," says Dederick. "Barring a sudden, sharp economic slowdown, the odds suggest that we are facing an appreciable pickup in inflation."

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RIGHT NOW, AN OUNCE OF PREVENTION IS ALL INFLATION NEEDS

BY ALAN S. BLINDER



A jump in prices from one month to the next means little. So until the monthly numbers begin to show a clear inflationary trend, Greenspan and the Fed are wise to ward off the problem with small doses of restraint and a large dose of calm

Talk of inflation is in the air again, as it should be—to a degree. Recent events suggest that America should now be on guard against rising inflation, but our policymakers should not be doing much about it yet. To explain why, it helps to know a little bit about both the government's inflation data and the theory economists use to interpret it.

First the data. The consumer price index (CPI) measures inflation by estimating the cost of buying a prescribed list of commodities at monthly intervals. If the cost of this "market basket" is \$1,000 one month and \$1,006 the next, we say the inflation rate for the month was 0.6%, or roughly 7.2% at an annual rate. That is precisely what happened from December, 1988, to January, 1989. And because monthly inflation rates had been running at 0.3% or 0.4%, it raised eyebrows.

However, not much should be made of the difference between 0.4% and 0.6%. For one thing, the cost of the market basket each month is only an estimate. For another, the price index we care about is seasonally adjusted (because we do not want to call it inflation when, for example, the price of watermelons rises between August and February). These and other features of the CPI introduce small but unavoidable errors into our measurement of inflation, errors that must be kept in mind when interpreting monthly data. Had the estimated increase in the CPI from December to January been only 0.2% lower, there would have been no inflation headlines.

ANXIETY ATTACKS. I do not mean to imply that the CPI actually erred in any particular direction, for I have no reason to think so. I do mean to argue that a jump in the annual inflation rate from 3.6% to 7.2% for a single month means little. Economists want to see several months of consistent data before declaring a change in the underlying price trend. Such data are not yet in hand, so any anxiety attacks over inflation are premature. However, recent data contain enough hints that inflation is starting to accelerate that it makes sense to be vigilant.

Now the theory. The inflation model to which most mainstream economists now ascribe is based on the concept of a "natural" rate of unemployment. According to this theory, inflation has a strong tendency to accelerate whenever unemployment is too low and to decelerate whenever it is too high. The level of unemployment at which inflation neither rises nor falls is called the natural rate of unemployment. If the theory is correct, two important practical questions arise. What is the natural rate of unem-

ployment? And how quickly does inflation accelerate when unemployment is below that level?

Economists agree more on the answer to the second question than they do to the first. The consensus is that inflation accelerates very slowly. According to one popular rule of thumb, if the unemployment rate is a full percentage point below the natural rate for a whole year, inflation would be expected to rise only about a half percentage point.

This muted reaction of inflation makes it difficult to pin down the natural rate numerically. Take the 5.5% unemployment rate of 1988 as an example. If the natural rate was 5.5%, as I argued about a year ago (BW—Feb. 15, 1988), the inflation should have remained constant. Since that is precisely what happened, my estimate was confirmed. Right? Well, maybe not. If the natural rate was really 6%, the theory predicts that inflation should have accelerated—but only by about a quarter percentage point. The difference between zero and 0.25% is easily swamped by other factors that can pull inflation down—such as energy prices rising much less in 1988 than in 1987. So the failure of inflation to decline can be interpreted as evidence that the natural rate of unemployment in 1988 was above 5.5%.

Now for the policy implications. If the natural rate really is around 6%, the current inflationary fears are not misplaced. But the proper reaction is vigilance, not panic, for inflation should gather steam slowly, leaving us plenty of time to react. On the other hand, the natural rate might be 5.5% or lower, in which case there is nothing to worry about. Finally, it is possible that the natural-rate theory is wrong. Some unconventional economic theories suggest that we can run a perennial high-pressure economy without accelerating inflation.

MORE OF THE SAME. Faced with all this uncertainty, what is a poor policymaker to do? Prudence should be the byword. Right now a prudent policymaker should assume that the natural-rate theory is correct, that the natural rate of unemployment is between 5.5% and 6%, and that small departures from the natural rate lead to even smaller changes in inflation. History may yet prove mainstream economists wrong on all three counts; this is not physics. But it would be rash for policymakers to assume the theory to be wrong at this time.

This analysis suggests that we adopt a policy combining a small dose of restraint with a large dose of patience. Fortunately, that is precisely what Alan Greenspan and the Federal Reserve Board have been providing. More of the same is called for.

ALAN S. BLINDER IS THE GORDON S. RENTSCHLER MEMORIAL PROFESSOR OF ECONOMICS AT PRINCETON AND AUTHOR OF *HARD HEADS, SOFT HEARTS*

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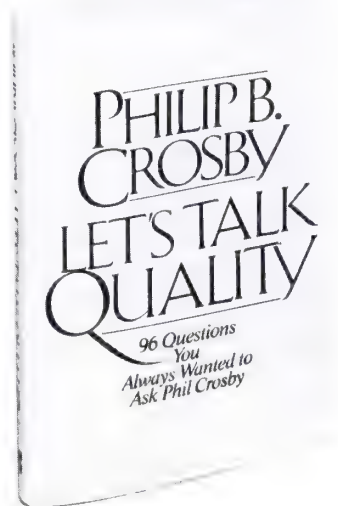
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INTEREST-RATE HIKES MAY NOT REALLY BITE 'TIL SPRING

Washington's latest batch of economic indicators shows that the expansion is still on track, and there are few signs of anything that might soon derail it. The only real impediment to growth is rising interest rates, but there's little evidence that credit-tightening by the Federal Reserve Board has slowed the economy. It will probably be spring before the effects of the February rate hikes can be gauged.

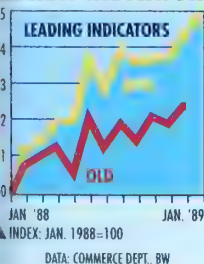
Higher rates will bite consumers first, but consumers are still a positive force in the expansion. And because hiring plans are strong through midyear—and income growth is accelerating—consumers are likely to keep borrowing and spending into summer. That will continue to fuel gains in the manufacturing sector.

GOOD NEWS FROM A DIFFERENT INDEX

For now, the Commerce Dept.'s new—but not so improved—leading indicators are strong, as are most measures of current business. The new index of leading indicators, designed to foreshadow the economy's performance, rose a strong 0.6% in January, following a 0.7% jump in December. Eight of the 11 components contributed to the increase, led by healthy gains in consumer expectations and stock prices.

Commerce has changed the mix of its leading indicators to include data that have better cyclical characteristics and are more timely. That's why it dropped two series: changes in inventories and in credit outstanding. Taking their place are measures of consumer expectations and inflation-adjusted unfilled orders at durable goods manufacturers. In addition, data on delivery times and materials prices were improved.

MORE MOMENTUM IN NEW INDICATORS



More reliable than the old one. Applied retroactively, the new index has signaled recessions about 9½ months in advance—the same average lead time as the old index. And despite the changes, it has still given two false warnings of recession, in 1984 and in 1987.

As with the old data, none of the new leading indica-

tors measures the services side of the economy, nor do they gauge the increasingly important role of global markets. These holes in the data caused the false signal in 1984. At that time, only the manufacturing sector, the victim of the superdollar, was in a slump, while services continued to power the expansion.

Although the new index has predicted recessions that didn't happen, it has never missed one that did. And that adds a glow to the outlook: The new index currently gives no signal of trouble. In fact, its vitality is echoed in the other composite indexes, which the government also revised. The coincident index, which measures current economic activity, jumped 1% in January.

More important, the ratio of the coincident index to the lagging index—which also turns down prior to a recession—has been climbing strongly and now stands at its highest in almost five years.

THE THRUST FROM EXPORTS IS WEAKENING

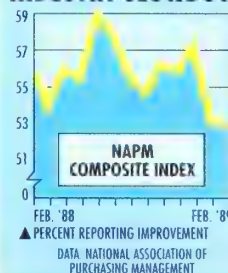
The latest readings on manufacturing aren't nearly as clear-cut. The factory sector in early 1989 seems to have retained much of the vigor it displayed during 1987 and 1988. That vibrancy stemmed from robust domestic demand plus an unprecedented kick from foreign demand. Through January, factory orders remained in a strong uptrend, and inventories are exceptionally low relative to the healthy pace of shipments.

For the rest of the year, though, domestic consumers will play an increasingly important role in the health of the manufacturing sector. Exports aren't growing as fast as they were, most likely because the dollar stopped falling last year. Indeed, the trade-weighted greenback is now slightly above where it was last spring.

That's probably the reason why manufacturing is starting to send out mixed signals. These likely reflect the recent slowdown in export growth, not the impact of the Fed's credit-tightening moves on the domestic economy. Real exports, adjusted for price changes, posted a 17% annual rate of growth in the first half of last year. That pace fell to 11% in the second half—and to only 8% in the fourth quarter.

The National Association of Purchasing Management's (NAPM) latest survey of industrial companies illustrates the slowdown. The Purchasing Managers' Index, a composite measure of orders, production, employment,

PURCHASERS SEE AN INDUSTRY SLOWDOWN



inventories, delivery times, and prices, fell to 53% in February (chart).

A reading above 50% indicates that business is still expanding, but the February reading was the lowest in more than two years. Yet it remains to be seen if this latest drop is meaningful. The index fell sharply last summer only to regain ground during fall and winter. In February the NAPM reported slower growth in new orders, production, and employment.

In particular, export orders continued to slow. Of the 69% of the companies in the survey that export, only 22% reported increases in orders from abroad, down from 28% in January. That figure was close to 40% last spring, and it has been in a sharp decline since August.

HIRING PLANS HIT A FIVE-YEAR HIGH

Slower export growth may be putting pressure on certain factory inventories. Stock levels rose a hefty 0.9% in January, to \$357.3 billion. That was faster than the 0.3% increase in January shipments, but sales in December had surged 2.8%. That means the ratio of inventories to shipments, though up slightly in January, is still historically low. But the ratio in nonelectrical machinery, a big export item, has been rising.

Inventories of finished goods in recent months have been growing far faster than stocks of materials and supplies. That may well reflect slower foreign demand for end products, but it is also the result of tight capacity farther back in the production sequence, which makes many supplies hard to get now. Capacity utilization in primary processing was nearly 90% in January.

Clearly, domestic demand is still strong, and this is offsetting slower growth in exports. So manufacturing will remain on the upbeat in coming months.

Right now, consumer fundamentals, particularly income growth and confidence, are firm, buoyed mainly by the bright job outlook. The latest quarterly survey of nearly 14,000 companies by Manpower Inc. shows that

hiring expectations for the second quarter are at their highest in five years.

When Fed tightening finally does hit, it will show up in the credit-sensitive, durable-goods sector of manufacturing. But so far, there are few indications of a slow down. Consumers still seem willing to add to their already heavy debt burdens to buy home appliances and furniture. And the Manpower survey shows no letup in hiring plans in durable-goods industries.

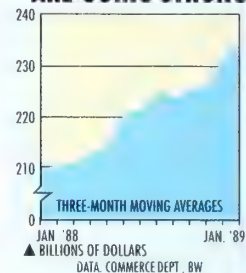
In addition, despite the slower growth in February orders reported by the NAPM, government data show that new orders for both durable and nondurable manufacturing remain in a solid uptrend (chart). Orders for household goods and apparel, which have been volatile, fell in January, but they have been moving irregularly higher for the past year. And orders for consumer staples, such as food, drugs, and toiletries, have accelerated recently.

Orders for automotive equipment have been trending higher since late 1987, reflecting Detroit's strong production schedules. But lately, auto output has been at odds with sales. Since October, auto production has averaged a 7.7 million annual rate, but sales of domestically made cars stood at 7 million in both January and February.

As a result, dealer inventories surged to an 85-day supply at the end of January, falling only slightly, to about 79 days, at the end of February. But if Detroit can thin out car lots with a new round of sales incentives, there'll be no need for production cutbacks.

That's a good example of why manufacturers remain most dependent on U.S. consumers—and of the trouble that may be in store later in the year, when higher interest rates do start squeezing consumer spending.

FACTORY ORDERS ARE GOING STRONG



THE WEEK AHEAD

RETAIL SALES

Tuesday, Mar. 14, 8:30 a.m.

Retail sales in February likely increased just 0.3%, held down by weak car purchases. In January, sales rose 0.6%.

MERCHANDISE TRADE BALANCE

Wednesday, Mar. 15, 8:30 a.m.

The trade deficit probably shrank to \$9.5 billion in January, from \$10.2 billion in December, on a customs-value basis. Rising oil shipments offset declines in other imports. Exports likely increased.

BUSINESS INVENTORIES

Wednesday, Mar. 15, 10 a.m.

The consensus of economists is that business inventories probably grew by

0.7% in January, after increasing 0.9% in December. Factory stocks already posted a 0.9% gain in January. Business sales should record a slim 0.3% gain in January, after a 0.8% jump in December.

HOUSING STARTS

Thursday, Mar. 16, 8:30 a.m.

Housing starts in February probably fell to an annual rate of 1.57 million in response to rising mortgage rates. Warm weather in January pushed starts to an unsustainable rate of 1.69 million.

INDUSTRIAL PRODUCTION

Thursday, Mar. 16, 9:15 a.m.

Industrial output probably grew by a slight 0.3% in February, following a 0.4% increase in January. A small rise in man-

ufacturing will slow February's overall gain. Because of the high level of unfilled factory orders, the current weakness is most likely temporary.

CAPACITY UTILIZATION

Thursday, Mar. 16, 9:15 a.m.

The small gain in output suggests that 84.3% of industrial capacity was utilized in February. That would be a slight loosening from January's 84.4% rate.

PRODUCER PRICE INDEX

Friday, Mar. 17, 8:30 a.m.

Producer prices for finished goods probably advanced a rapid 0.6% in February. Higher energy prices will lead the gain. In January, prices jumped 1%—the fastest increase in more than three years.

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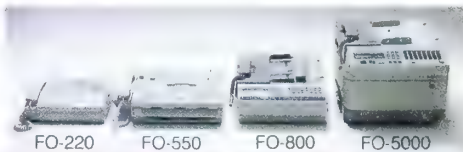
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THE TIME-WARNER DEAL

MARCH 20, 1989

KEEPING UP WITH THE MURDOCHS

THE GLOBAL MEDIA RACE FINALLY LURES TIME AND WARNER

Things haven't worked out quite the way Time Inc. founder Henry Luce imagined when he proclaimed this the "American Century." Luce's own publishing empire now must struggle to keep pace with fleet foreign rivals: West Germany's Bertelsmann, France's Hachette, Britain's Maxwell Communication Corp., and, perhaps most fearsome, Aussie Rupert Murdoch's News Corp. These giants have been reaching across oceans to snap up a publisher here, a record company there, an entire Hollywood studio. Meanwhile, back in the States, Time's compatriots have been mostly, well, selling out.

Now, Luce's corporate heirs are planning to reassert American power. On Mar. 4, Time, the nation's biggest publisher, disclosed a scheme to swap stock and merge with entertainment conglomerate Warner Communications Inc. The result, Time Warner Inc., will collect more than \$10 billion in annual revenues from an astonishing array of products and services: movies, TV shows, records,

magazines, books, and cable (page 34). Together that's enough to make Time Warner the world's biggest media and entertainment combine.

The Time-Warner combo won't immediately plant the flag in new turf abroad. But make no mistake, the deal's architects, Time Chief Executive J. Richard Munro, President Nicholas J. Nicholas Jr., and Warner Chairman Steven J. Ross, moved to blunt the foreign invasion—and to counterattack. "We're competing with the multinationals of many, many countries," Ross said. "Entertainment is probably America's No. 2 net export. Now we're No. 1 in that industry."

It will be intriguing to see if Ross, Munro & Co. can get their show on the road. But perhaps more crucial is understanding how infectious this global bug has become: The faithful—and the industry is loaded with them—hold that media and show biz are becoming more integrated and reaching farther around the globe. To survive, companies must build their operations and expand into new

fields—by costly acquisitions, if need be.

The evidence is everywhere. Take Japan's Sony Corp. It was a successful simply focused consumer electronics manufacturer—until last year, when it shelled out \$2 billion for CBS Records (table). Why? Sony Chairman Akio Morita had only to tune his Watchman to the evening news to see Japanese teens going wild when CBS recording star Michael Jackson played Tokyo. More important, owning CBS Records guarantees Sony control over a supply of music for its Walkman buyers. Better yet, take Murdoch: A few months back, News Corp. paid a staggering \$2.85 billion for Triangle Publications Inc. and its *TV Guide*—a magazine that neatly complements his growing Fox TV network.

And the beat goes on. Only days before the Time-Warner announcement Murdoch disclosed plans to raise more than \$1 billion to add new media properties to his newspapers, magazines, TV, and movies. Sony is interested in a major Hollywood studio. And Time's stock



soared beyond its supposed postmerger value as Wall Streeters wagered that another suitor might show up with a cash offer. Rumors are rampant: Is Paramount Pictures owner Gulf & Western going to merge with MCA? Will United Artists buy Columbia Pictures? Predicts Sony Corp. of America Vice-Chairman Michael P. Schulhof: "The price of any media company will rise" because of Time Warner.

DEAD AS DISCO? Media madness? No question, the agglomerations run contrary to today's management credo that companies should focus on core operations (page 36). And the new giants must find ways to bar the growth of a ponderous bureaucracy: If they don't, they'll soon be dead as disco. The winning approach, as Bertelsmann Chief Executive Mark Wossner puts it, is not to "seek size, but rather qualitative market-share leadership in the small, very differentiated, and highly sensitive media markets." With careful management—a tall order—the giants paradoxically may be the quickest to spot, sign, and market globally their ultimate profit sources: blockbuster authors, directors, singers, and actors.

While going global doesn't guarantee success, in more and more cases it's proving to be mandatory. For U.S. companies, to own a foreign distributor means not having to worry about being cut out of markets abroad—where the growth lies. To foreigners, stateside pro-

duction capacity means a tap on the only country that routinely makes and popularizes the films, TV shows, and music that sell worldwide. And don't forget the many ways to squeeze out extra profits: A book may lead to a movie, which then can be released on video. Then toss in a soundtrack record and, perhaps, promote the book-movie-video-record extravaganza in your magazines.

Inc. ran aground last year. Even Tri-Star Pictures, founded by heavyweights Time, CBS, and Coca-Cola's Columbia Pictures Entertainment Inc., has found the going rough. Columbia, which now controls the four-year-old studio, will soon subsume it.

TOPLESS TABLOIDS. In many ways, the man responsible for the frantic globalization of media is Rupert Murdoch. A decade ago he was known mainly for an imperial collection of tabloids featuring bare breasts and never-ending cash contests. Since then, Murdoch has turned his attention to entertainment's very heart: U.S. movies and TV. He began his TV empire in 1985, when he bought seven TV stations from Metromedia Inc. for \$2 billion. In 1986 he added Twentieth Century-Fox Film Corp. for \$1.55 billion.

The result: Murdoch now produces movies and TV shows that he can sell or air on his Fox network and Sky Television, his new European satellite venture. Should he choose to take the editorial risk, he

can publicize his productions to the hilt in his *TV Guide* and *Premiere* magazines. It seems to be working: News Corp.'s revenues surged to \$4.75 billion in the fiscal year ended last June, up from just \$1.64 billion in 1985. And in the latest six months, operating profit vaulted more than 31% on a 21% gain in sales.

With such a payoff, why haven't U.S. media moguls followed Murdoch down the acquisition trail? In some cases, their

GOING GLOBAL: MEDIA GIANTS' SHOPPING SPREE

Acquirer/Target	Date	Price	1988 Revenues
SONY/CBS RECORDS	JAN. 1988	\$2 BILLION	\$11.9 BILLION
TIME-WARNER	MAR. 1989	STOCK MERGER	\$8.7 BILLION
BERTELSMANN			\$6.2 BILLION
/DOUBLEDAY	SEPT. 1986	\$475 MILLION	
/RCA RECORDS	DEC. 1986	\$350 MILLION	
NEWS CORP.			\$4.35 BILLION
/FOX TV	MAR. 1986	\$1.55 BILLION	
/TRIANGLE (TV GUIDE)	NOV. 1988	\$2.85 BILLION	
HACHETTE			\$4.2 BILLION
/DIAMANDIS	JUNE 1988	\$712 MILLION	
/GROLIER	APR. 1988	\$450 MILLION	
MAXWELL/MACMILLAN	DEC. 1988	\$2.6 BILLION	\$3.3 BILLION*

*Estimate

DATA: COMPANY REPORTS, BW

Small is beautiful, you insist? Mega-deals turn into megaflops, you say? Look at the record.

Small outfits are having more trouble operating in the shadow of the giants. The No. 2 music publisher, SBK Entertainment World, recently decided it couldn't afford to stay independent and sold out to Thorn EMI PLC. Independent Hollywood studios such as De Laurentiis Entertainment Group and Cannon Group

path has been blocked: Murdoch and Robert Maxwell have firm control over their empires. Privately held Bertelsmann seems impregnable. And Sony, like other foreign buyers, could pay a higher price for CBS Records than a U.S. acquirer because of the weak dollar.

Moreover, it's prudent for most big American media companies to tiptoe overseas—particularly in TV. Although European programmers desperately want American shows to fill the airtime on their newly created private stations,

satellite channels, and cable services, a growing number of foreigners resent the bombardment of American culture. European Community ministers have agreed that a majority of their programs should come from Europe.

Many U.S. companies have footholds abroad via joint ventures. Trouble is, as an executive says at France's Générale Occidentale, which is looking for new media holdings: "There are a lot of operators around with a lot of money, but there aren't many deals left to do."

While they made it look as if they rushed into each other's arms, Time and Warner were pushed into the deal. A foreigners leapfrogged over American rivals by methodically snapping up U.S. assets, the two companies cast about for a quick way to reclaim the lead. They may have found it. But Time Warner won't stay out front unless it figures out how to play the globalization game at least as well as the giants from abroad.

By David Lieberman in New York, with bureau reports

THE TIME-WARNER DEAL

WILL IT HAPPEN? AND WILL IT WORK?

There's the risk of a raid, and synergies may be limited

Is the proposed merger of Time Inc. and Warner Communications Inc. a smart move? One of the industry's best-known empire-builders thinks he knows the answer: "For both companies, it seems to represent a safe haven from hostile threats, as well as synergism," says John C. Malone, president of Tele-Communications Inc., Time and Warner's chief cable competitor. "You've got to say: 'Wow, this is something else.'"

No gainsaying that, but it could turn out to be something else entirely. The gargantuan media merger may have been intended both to make its two parties takeover-proof and to create a Time Warner that's more than the sum of its parts. Yet there's reason for skepticism on both counts.

For starters, by three trading days after the wedding announcement, Time's stock stood at 114%, up 5¾ points on speculation by arbitrageurs that the publishing and cable company was still vulnerable to a hostile bidder. Some even speculated that Warner was at risk. "It's possible both companies are in play, and I'd say there is a greater than 50% chance someone makes a bid for Warner, not Time," says one arb. The list of rumored buyers came straight from the Hall of Fame: Nelson Peltz, Ronald Perelman, Robert Maxwell, Rupert Murdoch, Bertelsmann, and Gulf & Western.

As for synergy, the combination of distribution channels clearly offers opportunities to recycle the information and entertainment produced by the combined company's varied units. Time's HBO, for instance, wants to sponsor more original productions that it can air and then sell elsewhere—including on cassette through HBO Video. Warner is in an excellent position to feed that pipeline, particularly since it acquired Lorimar Telepictures Corp. in January.

But while it's easy to get starry-eyed about synergy, the reality is often sharp-

ly limited—as executives in other industries have sometimes learned to their grief. And in Time Warner's case, the deep cultural differences between the two parties—between New York publishing and Hollywood entertainment—may create serious obstacles. "It's like marriage where they agreed not to live together," says an investment banker. "I think they're papering over differences that are going to emerge later."

IN-HOUSE HEAVEN? That's not how Time and Warner see it, of course. In particular, Time CEO J. Richard Munro and President Nicholas J. Nicholas Jr. hope that the merger will solve a number of pressing problems. Wall Street has long been underwhelmed by Time's sluggish performance and the slow-growth prospects for its core publishing business. Prior to the merger announcement, the stock traded for under 110, even though many analysts figured the company break-up value was at least \$200 a share. If neither Time nor Warner snatched from the other's arms first, the merger would certainly leave the company less vulnerable—although the \$25 billion buyout of RJR Nabisco Inc. proved there's no one too big to be swallowed.

Synergy, too, looks a lot more promising from Time's Manhattan perch. One insider sketches an alluring scenario: "You get the book. It's serialized in a magazine. You can make a movie. Sell the video rights. Show it on Home Box Office. Feature it on your cable system. And then put the score on a compact disc."

It might work out that way. But such visions often run into real-world constraints in such notoriously competitive markets as publishing, broadcasting, and film. To survive, producers of information and entertainment must seek out the best at broadest audiences, whether not the parent's distribution and provides the channel. Similar publishers and broadcasters must seek out the best produc-

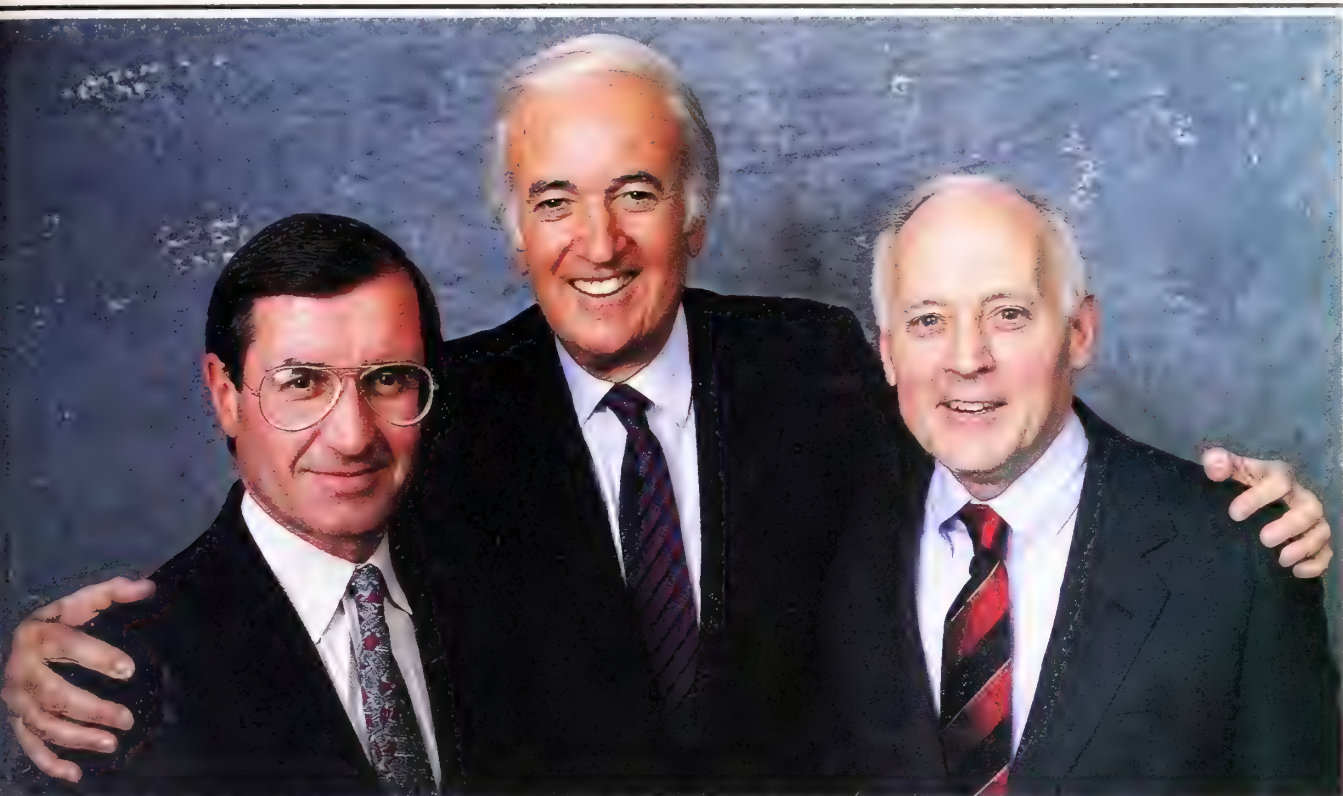
Time



INTRODUCING TIME WARNER INC.

Division	Selected properties	Revenues	Operating income
1989 estimates in millions			
PROGRAMMING AND FILMED ENTERTAINMENT	Warner Bros., Lorimar, HBO, Cinemax	\$3,420	\$490
MAGAZINE AND BOOK PUBLISHING	Time, DC Comics, Warner Books	2,925	435
MUSIC RECORDING AND PUBLISHING	Atlantic records, Warner/Chappel Music	2,400	370
CABLE AND BROADCASTING	American Television & Communications (82%-owned), Warner Cable Communications	1,450	335
TOTALS		\$10,195	\$1,630

DATA: MCKINLEY ALLSOPP INC.



NICHOLAS, ROSS, AND MUNRO: "IT'S LIKE A MARRIAGE WHERE THEY AGREED NOT TO LIVE TOGETHER. . . . THEY'RE PAPERING OVER DIFFERENCES"

A bad deal isn't made much better just because it's all done in-house.

On one count, there's little doubt that Warner can help Time—in cracking the vast and fast-growing overseas markets. That's something Time has had trouble doing: The company makes only 6% of its sales abroad. Warner's foreign distribution system, by contrast, is strong and growing stronger. The company already gets 40% of its revenues overseas, and that percentage is on the rise.

LONG FEUD. For his part, Warner CEO Steven J. Ross sees Time as adding a dose of stability to a clutch of businesses well-known for their sharp ups and downs. Publishing may not be as profitable as entertainment in good times, but the bad times aren't so rough.

For Ross, though, one of the deal's sweetest lures may have little to do with earnings. Many Warner watchers think he was drawn by the chance to neutralize Chris-Craft Industries CEO and Warner board member Herbert J. Siegel. The two men have been feuding almost from the moment Siegel rescued Ross from the clutches of Rupert Murdoch in 1984. Siegel became Warner's biggest shareholder and a leading critic of Ross's occasionally imperial style. He was also the only member of Warner's board to abstain on the merger proposal, which would dilute his holdings from 9.4% to 6%. "For Ross, it's a chance to stick it to Herb Siegel once and for all," says an investment banker.

Whatever the motivation, the giant deal had modest beginnings. About two

years ago, Ross approached Time with the notion of setting up a joint venture in cable. "I said: 'We have an idea, and can we waste some of your time?'" Ross recalls. By July, 1988, rumors about a possible Time-Warner cable venture were spreading—but the two sides were already hatching grander plans. Their discussions broke off just before Labor Day while Ross pursued Lorimar. And the Time executives had to decide whether they really wanted to go into the entertainment business. By Christmas they concluded they did.

If Time and Warner are to see much benefit from their combination, though, the ambitions that helped bring the companies together will have to be checked in the executive cloakroom. Architects of the merger agreement insist that they've anticipated and headed off any power struggle at the top. Ross and Munro will be co-chairmen and co-CEOs, with Nicholas as president and heir apparent in the ruling troika. Munro, 58, plans to retire at 60. The 62-year-old Ross also intends to step down in a few years, and insiders say he decided late in the talks to try to lure Nicholas as his successor if the companies didn't merge.

In general, Time's chiefs will have the final say over publishing and cable, while Ross keeps his kingdoms in film, TV production, and music. But skeptics think this division of power can't last. "You've got co-CEOs, co-chairmen, and probably co-security guards," says Raymond L. Katz, an analyst at Mabon, Nugent & Co. "It's definitely a problem."

Doubters say there's likely to be a clash of those "co's" sooner or later. Nicholas, 49, is a Harvard MBA, a strategic planner who has served as Time's controller and CFO. He's perceived as new blood—part of the generation that came up through Time's cable-TV ranks. And he's also known as "Nick the Knife": He planned the recent restructuring and cutbacks in an effort to slash costs at "Paradise Publishing."

EASY TOUCH. Ross began his career with his father-in-law's funeral parlor business, which he built through a series of mergers into Kinney Services and ultimately Warner Brothers Inc. He created his \$4.7 billion media and entertainment conglomerate by being a generous friend to his most important assets—the stars. Celebrities know he's an easy touch when they need a favor. And he's no tightwad with himself: In 1986, Ross negotiated a new compensation package that could eventually bring him more than \$180 million.

Personalities aside, there are also fundamental differences between the buttoned-down, Ivy League Time and the glitzy, entrepreneurial Warner. "One reason Time never went into records or movies is because they're terrified of the culture," says one investment banker. Whatever the risks, Time and Warner have opted to take a bold step into worlds neither knows. The matchup, at a minimum, will be something else to watch.

By David Lieberman in New York, with bureau reports

Commentary/by Judith H. Dobrzynski

GIANT STEPS TOWARD THE GLOBAL VILLAGE—OR AN EGO TRIP?

Globalization. Vertical integration. Critical mass. Synergy. Those were the grand concepts that J. Richard Munro, Steven J. Ross, and Nicholas J. Nicholas Jr. trotted out to explain the Time Warner Communications megamerger. Scrutinize those rationales, though, and you begin to wonder. Perhaps the more appropriate words that spring to mind are takeover protection, management aggrandizement, and business chess—the ongoing game in which, say, a Rupert Murdoch makes a move, and rivals counter or merely copy it.

The merger, if it's completed, will have some things going for it. The videos, records, magazines, and books that Time and Warner produce require a substantial up-front investment that doesn't get repaid immediately. Together, Time Warner will have more avenues through which to distribute the products. It can spread their costs and risk more widely—as well as increase the chances for blockbusters. And by merging with a stock swap, Time and Warner conserve cash—money they'll need to invest.

But there's plenty of room for skepticism about the basic premise of the combination: that tomorrow's media-and-entertainment companies will be global, vertically-integrated leviathans selecting talent from their stables and then making and distributing products all over the world.

FEW COKES. In the mid-1960s, Marshall McLuhan prophesied that better communications would turn the world into a "global village." More recently, technological advances and deregulation have been demolishing national market barriers. Yet local tastes remain strong. "Markets are becoming more specialized," argues economist Walter Adams, co-author of *The Bigness Complex*.

Advertising agencies learned that lesson when they tried to sell the concept of global ads. They found that there are very few Cokes in this world—most brands and most ads require tailoring to local preferences.

Now many agencies have backed away from the global-market concept. And that undermines any plans for worldwide, advertising-supported media networks. "Distribution will only go where advertising takes it," says Robert A. Alexander, a media consultant. "If there's a global market, it's a long way off."

Many packaged-goods companies no longer even consider the U.S. to be

might find movies in Time's books.

But vertical integration has become less compelling to many companies. And it's rarely applicable in the service industries, according to James L. Heskett, a service sector expert at Harvard business school. Service companies, which depend on people, normally try to maintain flexibility by contracting out for as much as possible.

SYNERGY. The "supply" in question may also resist what Time Warner has in mind. Some creative people are likely to balk at being sold like a commodity—packaged in various forms that meet corporate goals, not personal aims. "People are very independent about who they want to work for," says Alexander. "It might also cut out people who don't want to work for such a big company."

Then there's the big management problem: achieving the desired synergy. Both Time and Warner are highly decentralized, and the units have distinctly different personalities and cultures. Suppose Warner wants to turn a new rock-and-roller into the next Madonna. Will the editors of *People* agree to put the wanna-be on its cover? Will Home Box Office give her a cable special? If Time and Warner are like most decentralized companies, synergistic ventures are likely to be difficult even if they don't raise questions of editorial integrity.

Meanwhile, Time Warner will be giving up some things to get these cross-marketing possibilities. The combined bureaucracy will surely slow decision-making. Warner's strength hinges to a large degree on the high quality of its relationships with Hollywood's directors, stars, and writers—something HBO doesn't have. Will Warner's forte be transferred to Time, or will that strength be diluted?

Corporations have to take chances. But Munro, Ross, and Nicholas haven't made their global giant case convincingly. In the end, the Time-Warner merger, like many others, may prove to be a triumph of ego and entrenchment over business sense.



one market. Some now advertise their products with different campaigns for different parts of the country. Campbell Soup Co. even changes the way it makes soups and sauces to cater to regional American tastes.

Well, then, how about vertical integration? Traditionally, companies have integrated in order to gain control over a source of supply in a tight market. In Warner, with its strong ties to Hollywood's creative community, Time sees a captive source of talent for its cable systems, pay cable channel, books, and magazines such as *People*. Warner



GROUNDING: PILOTS CAUGHT LORENZO OFF GUARD BY BACKING THE STRIKE

AIRLINES

LORENZO IS RUNNING OUT OF CHOICES—AND TIME

He has 'days' to find a way to avoid bankruptcy, says an Eastern director

You can say this about Frank Lorenzo: He got the fight he wanted. For nearly three years, the Texas Air Corp. chairman sought to force a showdown with the machinists' union at Eastern Air Lines Inc. On Mar. 4 he finally got his wish, as 8,500 machinists went on strike. But his confident prediction that Eastern could fly through a walkout proved false when his pilots refused to cross the machinists' picket lines. Their defiance caught Lorenzo off guard, say Texas Air insiders. It also has backed him into the tightest corner he has been in since he bought Eastern in 1986.

Now, Lorenzo is searching for an alternative to bankruptcy. He has few choices—and precious little time to act. Says Eastern Director Kay McMurray: "I think a decision on which option to take has to be made within days." One thing seems certain: Lorenzo has little chance of returning Eastern to its former status as a national airline. Says an insider who thinks the carrier may be forced to declare bankruptcy: "You don't have an airline anymore, you have ashes." The same might be said for the

future time cards and paychecks of Eastern's 31,000 employees, for in this strike it's looking as if there will be no winners.

Insiders say that in a last-ditch bid to stay afloat, Lorenzo will probably keep trying to sell Eastern's assets piecemeal, as he has been doing for months. The unions know they would never get their



jobs back if that happened. So they're continuing to pressure Congress and the Bush Administration to set up an emergency mediation board. This would prevent Lorenzo from selling assets while the board devises a settlement.

If Bush doesn't budge, union financial advisers say they'll fight asset sales in court. They're trying to line up buyers

to join the unions in an offer for Eastern, and they're willing to make their pitch either to a bankruptcy judge or to Lorenzo, if he'll consider a sale. They've approached several groups since the strike began, including Trans World Airlines Inc. Chairman Carl C. Icahn, Grandview Acquisition Corp., headed by former CBS Inc. President John D. Backe, and Arthur E. Imperatore, a New Jersey trucking company owner, among others.

RUBBING THEIR HANDS. Meantime, Lorenzo is trying to cajole his pilots into going back to work. On Mar. 7 the pilots agreed to hold informal talks with Eastern. If, as seems likely, that fails, Lorenzo may be left with no choice but to declare bankruptcy. "This is probably his worst option," one union financial adviser insists. "It might trigger defaults at Texas Air. And we would try to take Eastern away from him in bankruptcy court." Why is organized labor drooling at the prospect of humbling Lorenzo—however hollow a victory that may ultimately be? Because it was Lorenzo who crushed the machinists and pilots at Continental in 1983.

Although Lorenzo could still snatch victory away from the unions by taking Eastern down with him, that promises little satisfaction. Without the Miami-based carrier, his dream of dominating the skies with a low-cost, nonunion airline could be over. His empire would be reduced to Continental, which isn't doing much better financially than Eastern. Continental lost \$315 million last year,

slashing its net worth from \$398 million to an estimated \$140 million. The company is expected to post a loss of more than \$50 million for the current quarter.

Just a year ago, Lorenzo seemed to hold all the cards: a pile of cash and elaborate strike contingency plans. Most important, Eastern's pilots were angry at Charles E. Bryan, leader of the International Association of Machinists District 100 at the airline. The IAM was the only Eastern union that refused to take a 20% pay cut in 1986.

But Lorenzo's strategy backfired. Eastern wouldn't budge on its IAM demands, which included pay cuts of up to 36%. This alienated the National Mediation Board, which refused to bring the confrontation to a head last year when

vately that up to half their members might keep flying in a strike. "It may be a no-win situation," explained 16-year pilot Frank Armstrong. "But if I can't have an airline, Frank Lorenzo can't either."

Union leaders still hope an emergency mediation board will prevent Lorenzo from liquidating Eastern. But they're having a tough time. President Bush refused to appoint a panel. And Congress hasn't rushed to take up the issue, which is turning into a partisan battle. The IAM had hoped to disrupt the national transportation system with sympathy strikes on the railroads as a way to pressure Congress and Bush to appoint an emergency board. But the courts so far have thwarted that tactic.

Company officials say Lorenzo is also trying to sell Eastern's South American routes, where partial service has been maintained. Or he may shift them to Continental. In addition, in recent weeks, Eastern has offered its main machine shop in Miami to such buyers as Ryder System Inc. And on Mar. 8, USAir Group Inc. agreed to buy Eastern's eight Philadelphia gates and some Canadian routes for \$85 million.

But even officials at both Texas Air and Eastern admit that a tag sale may not avert bankruptcy. Lorenzo still has cash to make payments on Eastern's \$2.3 billion in debt. Eastern has about \$275 million in the till, Texas Air about \$200 million, and Continental \$125 million, insiders say. But creditors may not wait. Some say they were blindsided when Lorenzo put Continental into bankruptcy six years ago. They vow not to get caught flat-footed again. Their bankruptcy lawyers are standing by. And lawyers in the case say Eastern has retained Harvey R. Miller, a top bankruptcy attorney. As one creditor attorney puts it, "Everyone's getting ready."

SITTING DUCKS? The unions, too, are bracing to stop Lorenzo in bankruptcy. "If it goes to bankruptcy, we'll file our own reorganization plan," says IAM adviser Brian M. Freeman. Adds another union adviser: "Then we'll ask the court trustee to remove Lorenzo."

Bankruptcy could put Lorenzo's other companies at risk. Analysts say that some Eastern debt is guaranteed by Texas Air, which could bring it into the fray. And Eastern owes \$750 million in pension obligations, which the federal pension agency can collect from both Texas Air and Continental if it can't get the money from Eastern.

The trouble for Lorenzo is that bankruptcy may be his only choice. On Mar. 7, Eastern managers in Miami were told that the company would file for bankruptcy that night if the company lost a suit attempting to force the pilots to return to work. The judge sided with the pilots. But the company quickly reversed itself and asked the pilots for a meeting. To buy more time, Eastern officials said they also would appeal the Miami judge's rejection of their suit.

Eastern's unions have scored a telling blow against Lorenzo. But that doesn't make them winners. Lorenzo may lose Eastern, but he can ensure that employees lose their jobs. With both sides fighting to a standstill, it seems little can prevent them from realizing their apparent death wish.

By Pete Engardio and Gail DeGeorge in Miami, with Aaron Bernstein in New York, Todd Vogel in Houston, and bureau reports



STRIKING MACHINISTS: SEEKING A PARTNER TO MAKE AN OFFER FOR THE AIRLINE

Lorenzo wanted. As the NMB tried to force a compromise, Lorenzo dug in his heels. He kept Eastern going by selling off pieces, weakening the carrier all the while. It lost \$356 million in 1988, and its market share fell to 7% from 9%.

Lorenzo's critical error seems to have been in alienating the pilots. The Air Line Pilots Assn. (ALPA) wanted job and seniority guarantees if Eastern were shut down or merged with Continental. Lorenzo nearly agreed to their demands. But at the last minute, he made what could turn out to be a fatal error. The day before the strike, Lorenzo shipped his pilots a videotape of himself offering some of the ALPA guarantees. But he failed to mention fresh demands for \$64 million in concessions and his refusal to guarantee pilots' jobs in a bankruptcy.

That incensed the pilots. Their near-unanimous refusal to cross IAM picket lines shocked even their own leaders, who just days before had predicted pri-

While they maneuver, Lorenzo is trying to sell more of Eastern. Officials at the Trump Shuttle, the new outfit set up by New York real estate developer Donald J. Trump, say Lorenzo is pushing them to complete the purchase of Eastern's shuttle, which is still flying. On Mar. 7 the Transportation Dept. gave Trump officials notice that they had cleared all hurdles to completing a deal. Says a Trump official: "We may be ready to pay Frank in a few weeks, which we would do whether there's a strike or not."

The unions say they'll fight in court to keep Eastern from selling assets

REPUBLICANS ARE THIRSTING FOR BLOOD'

The GOP's hard feelings over Tower will dog the 101st Congress

The rancorous Senate debate over John G. Tower's nomination for Defense Secretary may have claimed its first victim: No matter how it turns out, the Administration's hopes of forging a bipartisan consensus with congressional Democrats may be dashed.

To hear Bush tell it, he's still holding his hand out to the opposition. He has avoided the personal attacks on anti-Tower leaders, such as Senator Sam Nunn (D-Ga.), that could poison his relations with Congress. "This is just one item," says a senior White House official. "We're not going to let it change the President's attitude."

But events largely beyond the President's control may frustrate his efforts at conciliation. In the Senate, the bickering over Tower has strained relations between the two parties. And the partisan wrangling threatens to spill over into the House. Conservative Republicans, concerned that a House Ethics Committee investigation of Speaker Jim Wright (D-Tex.) will be a whitewash, are ready to pounce. "Republicans are thirsting for blood," worries a leading Democratic strategist. Add that to the general bitterness left by the recent defeat of a congressional pay raise, and the Tower affair becomes just one more ingredient in a volatile political brew.

IGN OF WEAKNESS. With Democrats in firm control of both houses, a bipartisan approach is Bush's only hope of advancing his agenda. "The Tower fight proves the Democrats can oppose the President with impunity," says Thomas Mann of the Brookings Institution. "He can't get Congress to do anything on his own." And the opposition is prepared to test Bush every step of the way. Democrats are drafting minimum-wage legislation that the Administration has already threatened to veto. While Bush agrees that action is needed on issues ranging from child care to environmental cleanup, the price tag will be more than he's willing to accept.

Bush advisers thought that their strategy of conciliation would play to the chief execu-

tive's strengths as a former congressman and a veteran Washington insider. Instead, it has been taken as a sign of weakness. "The White House is trying to play touch football, and they don't realize these boys up here are playing tackle," says a top Senate GOP aide.

What Bush needs more than anything is a quick victory. That would take some of the sting out of the expected loss of the Tower nomination and help refute charges that his Administration is floundering. Senate Republicans are pushing the Administration to move on to a more winnable fight—*contra* aid. Humanitarian assistance for the Nicaraguan rebels expires Mar. 31, and the White House is expected to unveil a new aid plan soon. The proposal has a good chance of passing both houses. And the President apparently would relish an opportunity to

slap down any congressional effort to force the government to intervene in the Eastern Air Lines strike (page 37).

But such opportunities are limited. There are no quick wins to be had in the budget battle, which promises to be a long and arduous dance between Budget Director Richard G. Darman and Democratic negotiators. It will be months before Bush's plan to rescue the ailing savings and loan industry gets to a vote in Congress. And new arms control initiatives are on hold until the Administration finishes a review of defense and foreign policy.

STUDIED INDIGNATION. Oddly enough, the area where the Tower battle may have the least impact on Capitol Hill is defense. Both Senate Armed Services Chairman Nunn and his House counterpart, Representative Les Aspin (D-Wis.), are centrists who tend to agree with the Administration on issues ranging from reducing strategic and conventional arms to Pentagon procurement reform. One reason the President may be so reluctant to attack Nunn is that he needs the Georgian's support to head off Democratic calls for deep cuts in military spending.

No such courtesy extends to Speaker Wright, who will find himself on the defensive when the Ethics Committee issues its report on alleged violations of House rules, probably by mid-March. If the report exonerates him of any wrongdoing, House Republicans have laid plans to stage loud protests for the next two years. And if the panel recommends sanctions, Democrats may try to oust Wright. Such turmoil may take some of the heat off Bush, who will stay out of the fight. But partisan rancor in the House can only stalemate Bush's programs. "It's liable to set off a very unpleasant chain of reactions," warns one White House aide.

But to keep the "new breeze" promised in his inauguration from turning into an ill wind, the President must advance a positive program. And here he is hampered by the meagerness of his legislative agenda. All he has offered so far are less costly versions of Democratic proposals. And his stumbling start is already raising questions about his effectiveness as a leader. If his Administration continues along the current path, bipartisanship in Washington may soon mean little more than letting the Democrats have what they want.

By Richard Fly and Douglas Harbrecht, with Dave Griffiths in Washington



TOWER ON THE SPOT: WILL JIM WRIGHT FEEL THE BACKLASH?

HENRY KAUFMAN: CORPORATE DEBT ERODES COMPETITION

It's a sign of how ingrained mergers and leveraged buyouts have become: Economist Henry Kaufman, who often rails against towering corporate debt, has agreed to become a limited partner in Gibbons, Green, van Amerongen, an LBO firm that just bought Ohio Mattress Co. for \$941 million. But Kaufman still worries about excessive debt. In an interview with Senior Writer Judith H. Dobrzynski, he outlined how it may change the U.S.

Q What is the long-term impact of excessive debt?

A As corporations become more leveraged over time, there's bound to develop a more intimate relationship between the debtor corporation and the creditor institution. Eventually the financial institution will have a much greater say-so as to who is going to be in senior management, product development, research, and so on.

Q Is this good or bad?

A This eventually leads to what I would call a social democracy, because it leads to greater concentration of economic and business and financial assets. And [it] decreases ultimately the competitive setting in a society.

Q Would that make U.S. companies more like German companies, which some say are more competitive because they can take a longer-term view?

A They are, and they are not [more competitive]. Germany may have a certain element of efficiency in its large enterprises, but it is not in the forefront of having young people rush out and form their own businesses. Neither is Japan.

Q So while we might gain in efficiency, we might lose in innovation?

A Yes, [and] there's a certain amount of growth that we would ultimately lose. And also, eventually, government will play a more intimate role with

the business and financial community.

This [shift from equity toward debt] tilts us eventually more toward economic and financial concentration. And it tilts us more to a social democracy rather than an economic democracy. An economic democracy is one in which the marketplace dominates. A social democracy is one in which the government is much more involved.

Q How long a process is this?

A It may take a decade or more before

share in the cost of the inefficiencies that will be created.

Q Are there any countertrends?

A The counterbalancing trends could be if we experience a very significant recession the next time around, and if that recession would come early in the 1990s rather than late in the 1990s. If it is a shallow recession, which it very well may be, I don't think we will really arrest this movement toward the absorption of greater debt.

Q What should we do?

A We certainly should use the tax structure to encourage the growth of equity—that is, remove the capital-gains tax, remove double taxation of dividends.

I also feel that deposit institutions whose deposits are insured should not be permitted to make marginal credit accommodations... whether it is LBOs or anything, it doesn't make any difference. When they do that, it really subsidizes the low-quality borrower.

Q Would you regulate that?

A Yes, I would suggest that if a deposit institution wants to make marginal loans, whether it's in mortgages or loans to LDCs or to low-quality corporations or to whom-

ever, then that should be made with noninsured deposits with a separate entity. It can say to the public, we will pay you a higher rate of return for this deposit, but the deposit is not insured.

Q How can we make up the taxes lost by changing the tax structure?

A There's a debate as to how much tax will be lost. Some say there's a loss; others say there's a gain in revenue. [But] I don't think this should be tackled on the basis of revenue lost. What is at stake here is the nature of our economic and social society over the long run. It's something much more fundamental, [yet] we're worried because there's a shortfall in the budget.



we see more of the foundations of this coming into place.

Q Is it inevitable?

A It's most likely that we will move in that direction because these are subtleties that move into a system. You take one step, and another step, and another, and then you just can't reverse it.

As you move into this system—social democracy—what you do is socialize costs. We're doing that right now, when the government is going to make sure that no depositor experiences a loss when it comes to the savings and loans. But we, the people, help socialize that cost. And so it will be as we create these bigger complexes. We will all

CAN GOODYEAR PULL OUT OF ITS SKID?

A profit slide and stalled expansion in Asia threaten its No. 1 spot

Tom H. Barrett doesn't want to be the man to lose Goodyear's 63-year standing as the world's No. 1 tiremaker. Yet less than three months after Barrett became chief executive, that possibility looks very real.

Goodyear Tire & Rubber Co. is in a lull. Because of sliding earnings in last year's second half, Barrett is under lots of pressure for short-term profit gains (charts). Meanwhile, foreign rivals are stepping up their investment in tiremaking, challenging the company to keep pace. The next few months will be critical. Besides trying to build a foundation in Japan and Korea, Barrett must get Goodyear back in gear in North America, where profits and market share have been slipping. As one close observer puts it, Barrett has "a tougher job than any chairman at Goodyear."

It's made more difficult by the stalling of Goodyear's crucial drive to become a bigger player in Asia with a new South Korean tire plant costing some \$250 million. That's particularly true since arch-rival Michelin has tire operations with partners in Korea and Japan. The company's troubles in Korea began in 1987, when Goodyear refused to take on a Korean partner, fearing it would be handing over critical technology. Chairman and then-CEO Robert E. Mercer figured Goodyear could overcome local opposition and go it alone. Although the Korean government approved the plant a year ago, it imposed so many restrictions that sources say financing it was all but impossible. Now, Goodyear appears to be seeking a joint-venture partner after all, possibly Korean petrochemical giant Sunkyong Ltd., according to industry sources in Seoul.

DRIVE TO INVEST. Although Goodyear insists that it's going ahead with the plant, it hedges in a written statement, saying: "The current labor unrest and anti-American sentiment is a concern. If they don't change, then we may have to rethink our plans." Curiously, its freshly printed annual report makes no mention of the plant—even though it discusses other, much smaller plant expansions.

Goodyear's \$3.6 billion debt load, most of it taken on to buy back shares after Sir Jimmy Goldsmith's raid in 1986, could also account for its Korean retrenchment. Yet that debt hasn't dampened Goodyear's overall drive to invest. It plans capital spending of \$900 million

this year, a \$150 million increase from 1988 and more than most outsiders had predicted. Barrett is determined to spend on research and new capacity, despite the misgivings of some on Wall Street.

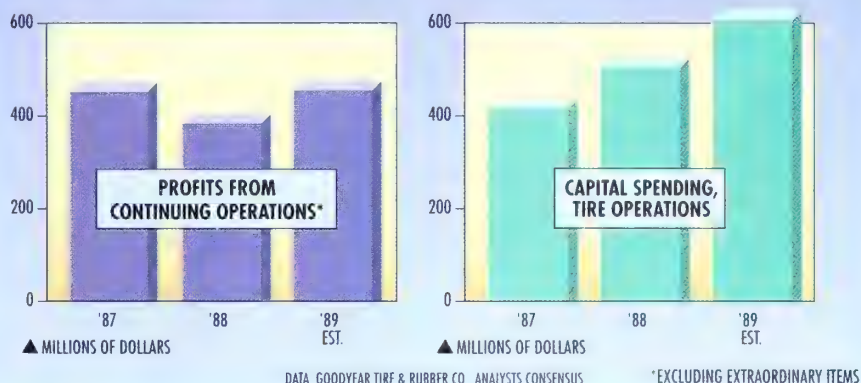
In fact, Goodyear appears to have decided that long-term industry leadership is more important than its oft-repeated goal of reducing debt to 50% of capitalization by the end of this year, down from 64% at the end 1988. A Goodyear

his control, last year produced 56% of Goodyear's profits on just 41% of its sales.

Higher raw materials bills hampered U.S. operations last year, slashing tire margins. Goodyear couldn't hike prices enough to compensate, and Detroit actually wound up paying 1% to 2% less than the year before for its Goodyear tires. Worse, Goodyear was unable to make enough tires to meet demand, so it lost U.S. market share and wound up selling more low-profit tires at the expense of lucrative models. Because of the weak results at home, Goodyear's earnings from continuing operations fell 14%, to \$377 million, on 1988 sales of \$10.8 billion. The problems came in the second half, when operating income fell 36%.

Sardas is moving to boost productivity and plans more layoffs. That hasn't

GOODYEAR'S WEAK EARNINGS AREN'T CRIMPING CAPITAL SPENDING



spokesman argues that meeting the 50% target has always depended on the sale or profitability of its California-to-Texas oil pipeline, which Goodyear has had on the block since Goldsmith's raid. And the company is using its cash to expand rather than to pay down debt. Remarks one lender: "They're going to have a lot of debt on their books for many years."

Barrett is depending on Jacques R. Sardas, the Egyptian-born executive who took charge of Goodyear's worldwide tire operations last August, to turn around the lagging North American tire business. The hard-driving Sardas has a good track record. Goodyear's international units, most of which were under

helped morale, which has yet to recover from last year's reorganization into global business units. "It has gnawed at the roots of the company," says one recent Goodyear defector. Both Sardas and Barrett declined to be interviewed for this article.

Sardas hopes to produce bigger profits from Goodyear's strong U.S. franchise by raising prices and cutting discounts. Although some customers reacted by trimming purchases, the higher prices look as if they have a reasonably good chance of sticking: Other tiremakers are following suit. And many customers remain loyal. "I'm convinced what Goodyear is doing is correct," says Terry Dapper, a big Goodyear wholesaler based in San Diego.

If the price hikes work, Goodyear's profits could surge in the second half, notes analyst Saul H. Ludwig of Cleveland's Roulston & Co. If they don't, Goodyear's net will suffer, and Barrett may earn Akron's most dubious honor.

By Zachary Schiller in Cleveland, with Larimi Nakarmi in Seoul

Goodyear's higher prices look as if they have a good chance of sticking: Other tiremakers are following suit

AT&T UNCHAINED: BUSINESS MAY BE THE WINNER

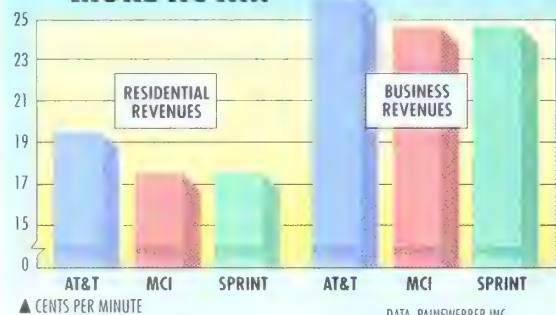
FCC plans will make the giant more profitable—and freer to compete

Uncle Sam is taking the leg irons off AT&T. After almost 60 years of strictly regulating AT&T's profits, the Federal Communications Commission is set to make a sweeping overhaul of the way it supervises the nation's largest communications carrier.

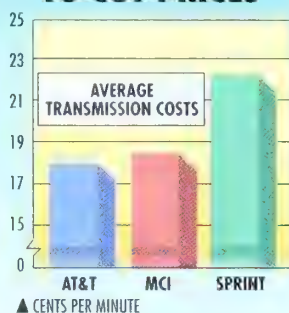
The changes could make the company a lot more profitable and give it more

decline in costs, it "can achieve returns of 25% to 30% on equity, even while reducing rates by 5% to 6% a year," he predicts. One way: Given the fast growth in such high-margin businesses as facsimile transmission, international calling, and 800 service, AT&T could make small price cuts for business services and still profit, analysts say.

ALTHOUGH AT&T CHARGES MORE NOW...



...IT HAS MORE ROOM TO CUT PRICES



flexibility to compete with its rivals. But the FCC's plans could also make for some pretty unhappy phone customers.

Most disgruntled may be residential customers, who probably won't see their long-distance bills continue to slide. Since the breakup of American Telephone & Telegraph Co. in 1984, average prices for service have declined by 39%. But increasing AT&T's ability to compete with lower-priced rivals such as MCI Communications and U.S. Sprint Communications should please the majority of business customers.

HUGE WINDFALL. The most important changes are to come at a meeting scheduled for Mar. 16, when the FCC is expected to junk its practice of regulating AT&T's rate of return on investment, now set at 12%. Instead it will cap the company's prices (charts). In theory, if cost cuts boost AT&T's profits, AT&T and its shareholders will be able to keep the gains instead of passing them back to phone customers in the form of price reductions.

The windfall could be huge. AT&T earned \$1.8 billion on its long-distance business in 1988. That, says PaineWebber Inc. analyst Jack B. Grubman, translates into a 20% return on equity. If the company tracks the industry's general

MCI and Sprint could benefit, too. They won't have to beat rate cuts that the FCC has imposed on AT&T to keep the \$35 billion carrier's profits within its allowed rate of return.

All of this makes it likely that the FCC's long-awaited rate-cap proposal will breeze through. Chairman Dennis R. Patrick has already mollified House Energy & Commerce Committee Chairman John D. Dingell (D-Mich.) and telecommunications subcommittee Chairman Ed-

ward J. Markey (D-Mass.) by deferring plans to extend the price-cap concept to the Baby Bells. Some lawmakers believe that AT&T's former phone companies still require strict regulation, given their monopoly in local service areas.

Patrick also agreed to keep AT&T from offsetting any cuts in business rates with higher residential prices. He proposes to keep price increases at least three percentage points below the inflation rate, with an overall cap of 5% on any service and 2% for residential rates.

But another plan may have more trouble. AT&T is currently the only long-distance company required by law to file with the FCC a public document—available to its rivals—that details its costs and rates for each service. Now the commission, in a regulatory shift that's not yet formally approved, is letting AT&T disclose minimal information and offer customized rates as it bids on lucrative multiyear service packages for big corporations.

UNEQUAL GAINS. Two of the FCC's three commissioners—Patrick and James H. Quello—are said to back the regulatory relaxation. But Patricia Diaz Dennis isn't satisfied that the FCC has followed proper procedures in allowing AT&T so much pricing freedom and could hold out a vote by demanding more public debate.

Dennis isn't the only dissenter. MCI and Sprint have threatened lawsuits, saying relaxed pricing rules amount to a backdoor way to deregulate AT&T. Capitol Hill also questions Patrick's plan to apply looser regulations to big business phone pricing than to residential rates. "You can't have AT&T deregulated for the large-end business customers and price caps for the rest of them," says a aide to Markey.

But that's exactly what Patrick intends to do. And it doesn't look as anyone will be able to stop him.

By Frances Seghers in Washington

HOUSING

CARDINAL'S SHAKY FOUNDATION

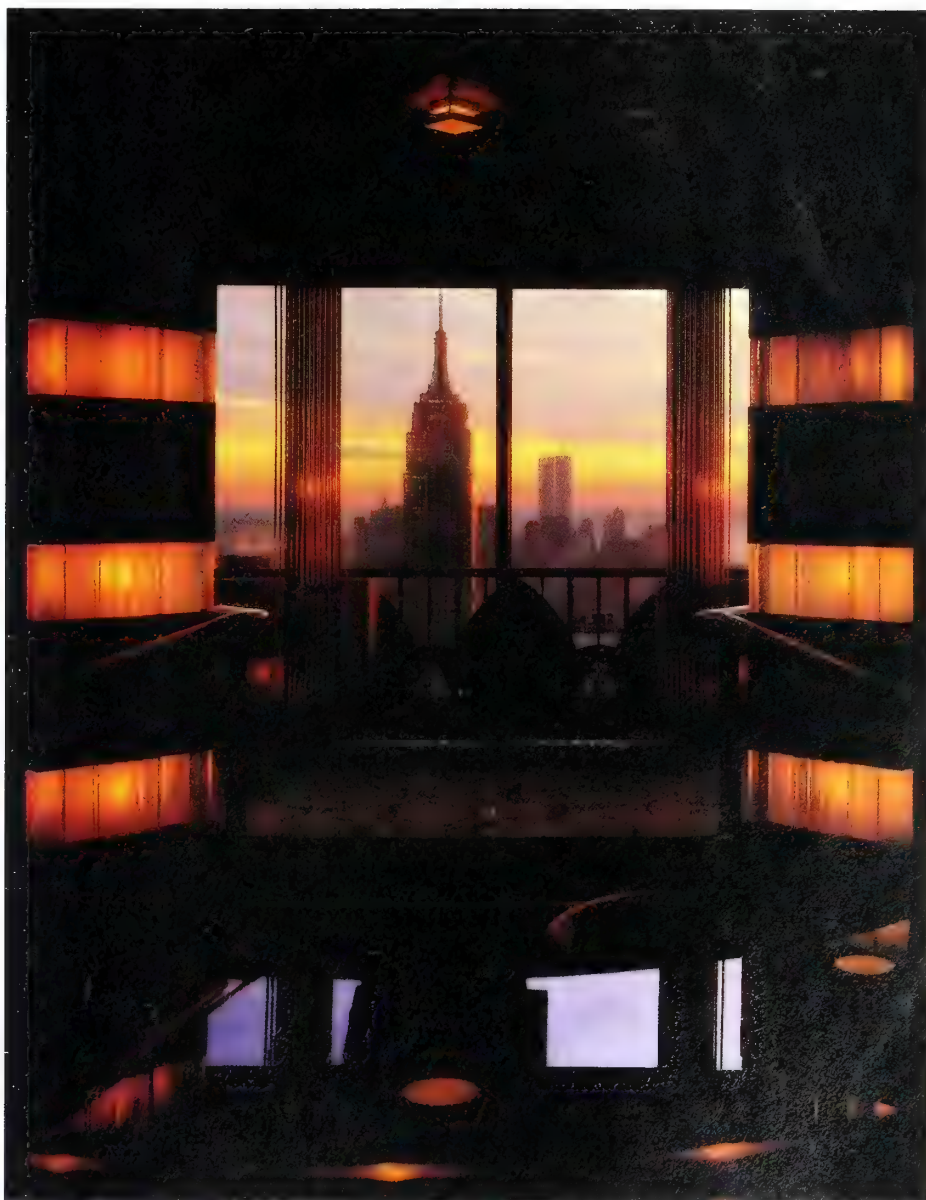
The homebuilder's lenders worry

Chairman Austin Guirlinger of Cardinal Industries Inc. has long been known as the housing industry's Henry Ford. By applying mass production techniques to construction, his Columbus (Ohio)-based company cranked out motels, apartments, and single-family houses by the thousands.

But now the nation's second-largest homebuilder may face a plague worse than termites. On Feb. 13, Guirlinger found himself hat-in-hand before more than 150 bankers in a Columbus hotel. His plea: forbearance on nearly \$8 million in monthly interest payments. He also asked creditors to extend Cardinal's \$55 million line of credit while it tries to unload \$45 million worth of apartment complexes and other properties.

TAX REFORM TOLL. But some lenders are balking. "We're always willing to listen to what they have to say, but they need a more specific plan," says Gary A. Glaser, chief executive of BancOhio National Bank, a creditor. And at the beginning of March, three of Cardinal's lenders began foreclosure proceedings on eight

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properties owned by a Cardinal subsidiary. If Guirlinger can't whip up a plan soon, other banks may follow suit.

That's quite a slide for a company that once prided itself on building and managing properties and financing them through the sale of limited partnerships to the public. What happened? Tax reform. Before the 1986 changes, high-bracket taxpayers invested in rental property to take advantage of juicy deductions. Tax reform tightened the rules, cutting Cardinal's revenues from syndicating the limited partnerships.

Despite the obvious threat that the new tax law posed, the 62-year-old Guirlinger blazed ahead. He opened a fifth

plant to build more of the 12-by-24-foot modules that Cardinal uses in its apartments and motels. He figured he could create new markets for the structures by expanding the company's then-profitable Knights Inn motel construction and management business. He also started developing retirement centers and rental properties that could be sold to the public through real estate investment trusts.

The bet hasn't paid off. Although Cardinal has almost doubled its stable of 100 motels in the past two years, many of the new sites are in poor locations. Says a former official: "Knights Inn motels are sucking wind and bleeding cash flow." Financial figures are difficult

to obtain for privately held Cardinal. Guirlinger insists that the company's woes are temporary, that once property sales are completed, Cardinal can pay the banks and restructure. "Chapter 11 is definitely not in our plans," he says. "We're asset-rich but cash-poor." May be. But creditors want a clear plan.

Guirlinger has shown he's willing to take drastic steps. In the past three months he has closed four plants and cut the number of employees working for the parent company to 1,000, from 3,300. But if he fails to convince his creditors, the Henry Ford of housing could end up more like Preston Tucker.

By Steve Phillips in Cleveland

STRATEGIES

BOB TAYLOR WANTS TO WALK AWAY FROM HIS OBSESSION

Why he's shopping perfume marketer Minnetonka

"It's my baby," says Robert R. Taylor, the founder and chairman of Minnetonka Corp. And my, how it has grown. Its first product was soap balls that Taylor rolled in his garage. Today, 25 years later, its mainstays are Calvin Klein's perfumes, Obsession and Eternity, which last year racked up an estimated \$140 million in U.S. sales.

Taylor would dearly love to see his baby grow to \$1 billion in annual sales, from \$213.5 million last year, but he realizes that it may be time to take the money and run. Fragrance companies are changing hands at record prices: Anglo-Dutch Unilever PLC, for instance, recently acquired Fabergé for about \$1.5 billion, or 1.9 times annual sales. Minnetonka may never look more attractive. So on Mar. 2, Taylor announced he had hired Morgan Stanley & Co. to explore the sale of Minnetonka. That sent the company's stock up 8 points, to 21½. Days later, rumors of a \$25 bid pushed the stock up another few notches.

Explaining his move, Taylor made the now-familiar bow to maximizing shareholder value. He would do a bit of maximizing for himself, too: His 6.7% stake is now worth more than \$26 million. Perhaps

just as important, the sale would extricate Taylor from an uneasy relationship with designer Calvin Klein, who with his partner, Barry Schwartz, holds 14% of Minnetonka's stock. Taylor says his relationship with Klein has improved, but Klein's own obsession with every aspect of his fragrances' production and marketing remains fierce. Neither Klein nor Schwartz would comment.

STAYING POWER. Taylor also may be trying to sell Minnetonka because it was falling out of Wall Street's favor. Days before his announcement, Minnetonka traded well below its six-month high of 18¼, reflecting the company's expecta-

tion of a loss in this quarter and the market's fears of slower growth ahead for Obsession.

Obsession and Eternity are, with Giorgio, still among the top three department store brands. But, warns industry consultant Allan G. Mottus, "the best news is already out." Demand for Obsession for women, introduced three years ago, shows signs of leveling out at \$55 million in sales, although Obsession for Men is still growing. The company's new floral fragrance, Eternity, has started out as a big hit. "Eternity was the launch of 1988," says Allen K. Burke, perfume buyer at Dayton Hudson Corp.'s department stores. Some observers think it may lack the two Obsessions' staying power.

It may take a while for a buyer to emerge, though Taylor expects to find one within 90 days. Would Klein consider buying his most profitable licensee? He said as much in Securities & Exchange Commission documents filed in 1987. But many analysts think that Min-

netonka, which may fetch more than \$40 million, or 27 times 1987 earnings, has become too pricey. Companies that might be interested, such as Avon Products Co. (page 123), may also be too debt-laden to swing the deal. Complicating matters, Klein's cooperation is key to Minnetonka's success.

Whoever wins the company will gain control of some powerful brands. But the new owner will need a formula for steady success in a market that's so fickle even obsession become passing fads.

By Mary J. Pitzer in Bloomington, Minn.



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EDITED BY HARRIS COLLINGWOOD

SIR JIMMY HEADS FOR HOME

► Embattled U.S. executives can rest a little easier. Anglo-French raider Sir Jimmy Goldsmith, the scourge of many a boardroom this decade, is taking his dealmaking back to Britain. After making a fortune in a string of takeovers and an aborted run at Good-year Tire & Rubber, Goldsmith reckons that the U.S. market is now too rich even for his taste. So he's hooking up with longtime pal Jacob Rothschild and his publicly traded Anglo Leasing to create a takeover machine in Britain, where corporate raiding is still in its adolescence.

The pair will target a wide range of nonfinancial companies that have lost their way through diversification. Presumably, Goldsmith also figures that under Prime Minister Margaret Thatcher, the union-plagued, left-leaning country he sold out of 10 years ago has changed enough to welcome his swash-buckling brand of capitalism.

GRAND MET SHAKES UP PILLSBURY

► Grand Metropolitan has put the Pillsbury Doughboy on a crash diet. The British company said on Mar. 6 that it will fire 550 employees at Pillsbury's Minneapolis headquarters—23% of the total staff. On Mar. 8 Grand Met announced it would sell Pillsbury's Steak & Ale restaurant chain to senior management for \$431 million. Grand Met, which bought Pillsbury late last year for \$5.7 billion, will plow the proceeds into its food operations and the ailing Burger King fast-food chain.

LEVI STRAUSS AND UPS NAME NEW CHIEFS

► Two of the more idiosyncratic U.S. companies are making changes at the top. At

Levi Strauss Associates, Chief Executive Robert Haas is replacing his uncle, Peter Haas, as chairman. LSA, created in a 1985 leveraged buyout, is six years ahead on its debt-repayment schedule and has posted, the company claims, record earnings in two of the past three years.

Vice-Chairman Kent "Oz" Nelson, 51, will become chairman and CEO of United Parcel Service within the next year, when John Rogers, 55, retires to a seat on the board. Rogers, in the job only since May, 1984, is emulating his predecessor, George Lamb, who also retired after five years. The privately held \$11 billion company makes almost a religion of consensus management, promotion from the ranks, and making room at the top. Nelson started with UPS right out of college in 1959.

FIRST UNION BUYS A FLORIDA BANK

► One of banking's most prolific acquirers has struck again. First Union, which has snapped up 20 banks since the U.S. Supreme Court's 1985 approval of regional mergers, agreed on Mar. 6 to pay \$749 million for Florida National Banks. First Union, based in Charlotte, N. C., will pay \$100 million more for warrants held by Chemical Bank, which has been sitting patiently on a five-year-old pact to acquire

TATERS TRY SOCIAL CLIMBING

Americans are justly famous for forgetting their differences and pulling together in times of crisis. Now is such a moment. For the first time in memory, U.S. per capita potato consumption is down. According to market researcher Packaged Facts, each American will eat 123.6 pounds of potatoes in 1989, down from 123.9 last year.

What's hurting the popularity of the humble spud? Gourmet starches such as pasta, that's what. But U.S. potato growers are fighting back by going upscale. On the cutting edge of tuber technology is James Huston, whose Yukon Gold potato has won raves from such epicures as Joel Robuchon, chef-owner of Jamin, a four-star Paris restaurant, who praises its taste and deep yellow hue. And like all potatoes, it's nutritious. As Packaged Facts President David Weiss says: "If bread is the staff of life, potatoes are the motorized wheelchair." You can't argue with that.

Florida National's \$7.8 billion in assets. Chemical can't move until Florida opens its doors to New York banks—and that won't happen any time soon.

THE MARKET PUMMELS MICROSOFT

► Wall Street didn't take kindly to Microsoft's Mar. 7 warning that quarterly revenues and earnings would be down for the quarter ending this month, the first decline in its three years as a public company. The software maker's stock lost 13% of its value, tumbling 8½ points, to 53½.

The market probably over-



reacted. The depressed earnings shouldn't last past the current quarter, since they stem mainly from last-minute delays in new versions of its word-processing program originally due by January. Microsoft now promises to ship the program in April. But investors, burned by such software delays as Lotus Development's year-late upgrade of 1-2-3, are in no mood for such surprises.

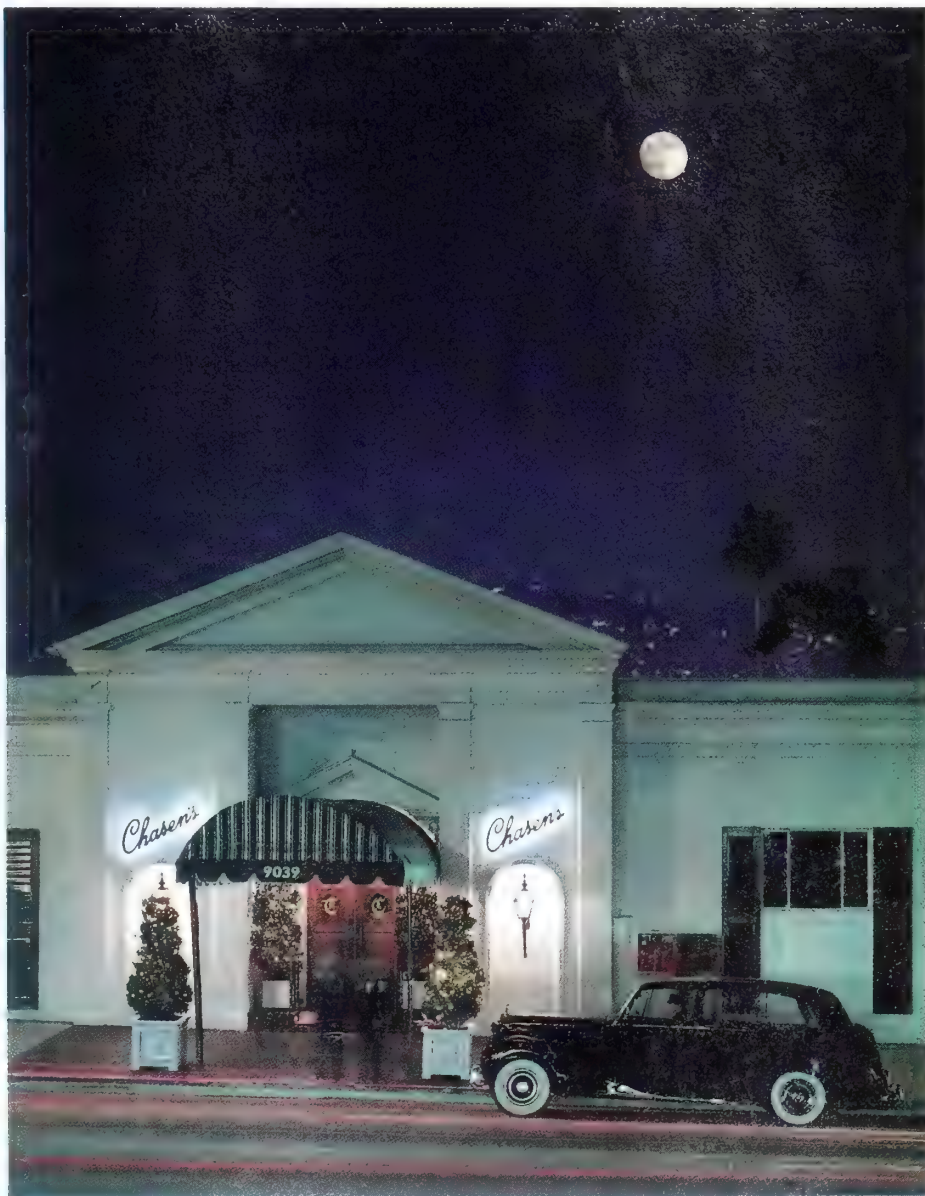
A KING-SIZE PRICE FOR OHIO MATTRESS

► Stashing money in the mattress has paid off for shareholders of Ohio Mattress. New York merchant banker Gibbons, Green, van Amerongen will pay \$25.50 a share for the Cleveland-based bedding company, which put itself on the block back in November. The price is more than what most analysts had anticipated.

Chairman Ernest Wulige will stay on and run the company once the \$941 million buyout is complete. Gibbon Green, along with its minority partner, Madrid's F. L. Botere, intends to expand the company's Sealy and Stearns & Foster brand names in Europe.



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open motorcar.

Equally rare is the silence and smoothness of Jaguar's fuel-injected, overhead cam V-12. With 262 horsepower, it is also one of the world's most potent production engines. Modified for racing, in 1988 it powered Jaguar to victory in the world's toughest 24-hour races—Daytona and Le Mans.

The XJ-S convertible moves with the uncommon agility and confidence of Jaguar's four-wheel independent suspension. It stops with the authority of one of the most advanced anti-lock (ABS) braking systems.

A car for all seasons, its beautifully tailored power top glides up or down in as little as 12 seconds. The top is luxuriously padded, fully lined and incorporates a heated glass rear window. Inside, the XJ-S climate control system automatically regulates heating and air conditioning. Its new sports-contoured seats

incorporate power-variable lumbar support and electric heating elements.

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JAGUAR XJ-S



HOW GEORGE BUSH MAY RECAST QUOTAS ON STEEL IMPORTS

On the eve of last fall's election, George Bush wrote to Senator John Heinz (R-Pa.) to say, "I can assure you of my intention to continue" quotas on steel imports. The well-timed promise matched an earlier pledge by Massachusetts Governor Michael S. Dukakis and helped Bush to a narrow victory in Pennsylvania.

Now the steel industry is calling in its marker. Despite strong sales and soaring profits, steelmakers are asking for a five-year extension of the 1984 Voluntary Restraint Agreement (VRA), which limits imports to about 20% of the U.S. market. The idea is popular on Capitol Hill: A bill urging the Bush Administration to negotiate an extension before the Sept. 30 expiration of the current pact has already gathered 52 co-sponsors in the Senate. And some of the 29 countries covered by the VRA are eager to sign up again, since inclusion effectively guarantees them a piece of the U.S. market and protects them against trade retaliation.

Sounds like a done deal. But in fact the industry will probably get an extension only after a protracted fight. And even then steelmakers will have to settle for a good bit less than they're asking for.

The steel dispute marks an early test of the Administration's intentions on trade. And the signs suggest the President's heart really isn't in the VRA. In his letter to Heinz, Bush noted that the only permanent solution to the domestic steel industry's problems "lies in negotiating an end to foreign subsidies."

SAFE HARBOR. U.S. Trade Representative Carla A. Hills is taking that suggestion seriously, much to the dismay of VRA supporters. Commerce Secretary Robert A. Mosbacher, while strongly backing a VRA extension, also favors finding a way to ease its impact on steel users. A Cabinet-level decision is not scheduled until the end of April.

Rather than immediately opening talks with the current negotiators, the Administration is considering a number of approaches that steel producers fear would dilute the agree-

ment's effectiveness. One possibility is a shorter extension of the VRA, perhaps for as little as two years.

Another point of contention is the treatment of countries that "dump" steel in the U.S.—selling it below the price in their home markets or at less than the cost of production. Because the current VRA gives exporters a safe harbor from dumping charges, one option is excluding the worst dumping offenders from the agreement so that the threat of higher duties or other antidumping penalties might force them to reform. South Korea, a constant target of complaints from the industry, has already served notice—along with Australia—that it would rather take its chances with antidumping suits

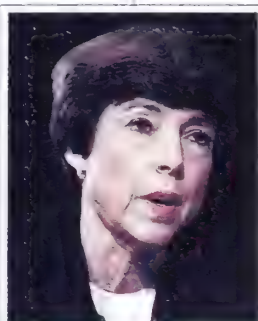
than sign up for a new VRA. Another possibility: Parties to the VRA might have their quotas expanded in return for promises to end subsidies.

Of even more concern to the steel producers is a proposal pushed by a coalition of steel users, led by Caterpillar Inc. The agreement now allows the government to waive quotas for items in short supply. The users want to expand waivers to cover products whose prices are moving up. But such a step would "abrogate the entire program," argues Richard P. Simmons, chairman of the Specialty Steel Industry of the U.S.

Steel customers have inflation fears on their side. "When you restrict the supply of a raw material from just a few producers to a wide number of manufacturers, your trade policy turns out to contradict your macroeconomic policy," says Paula Stern, former chairman of the International Trade Commission and a consultant to the steel users group.

Bush will keep his promise to give steel protection—in some form. But the situation has changed dramatically since 1984. The U.S. economy has grown more dependent on exports, and the Administration will be loath to cripple manufacturers by forcing them to pay more for steel. Look for the White House to do as little as it can get away with.

By Paul Magnusson



CARLA HILLS

CAPITAL WRAPUP

THRIFTS

The Federal Deposit Insurance Corp., says one Wall Street wag, is like the dog that finally catches up to the car: Now what does he do with it? Having acquired the responsibility for disposing of 200 moribund savings and loan institutions, the FDIC is looking for ways to peddle them to buyers. The insurance fund doesn't want a repetition of last year's highly criticized sales by the Federal Home Loan Bank Board. Instead of offering subsidies to buyers, the FDIC is more likely simply to discount the selling price. That at least would cut the government's future exposure. Another option: busting

up some sick thrifts and selling off the pieces. But no assisted sales will occur until Congress pumps some money into the S&L insurance fund.

THE SENATE

John H. Sununu, who's off to a rocky start as White House Chief of Staff, says he's not interested in running for the Senate seat being vacated by Republican Gordon J. Humphrey of New Hampshire, who is retiring. But GOP strategists aren't quite convinced. The election, says Wendy DeMocker of the Republican Senatorial Campaign Committee, "is still nearly two years away. Arms can be twisted." Sununu has long been interested in trying for the

Senate, but going for the seat would probably require him to give up his White House job early next year. Although former Governor Sununu is the state party's favorite, the GOP is likely to hold the seat no matter who runs.

NEW YORK

Former U.S. Attorney Rudolph W. Giuliani has hired a top Bush campaign aide as a consultant for a possible race for mayor of New York. Rich Bond and his partner, former White House political director Frank Donatelli, will map strategy for Giuliani's expected bid. With Democrats deeply split, Republicans think they have their best chance in years to win city hall.

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IN EUROPE, INFLATION IS NO LONGER DISTANT THUNDER

Interest rates go up, but consumers keep spending

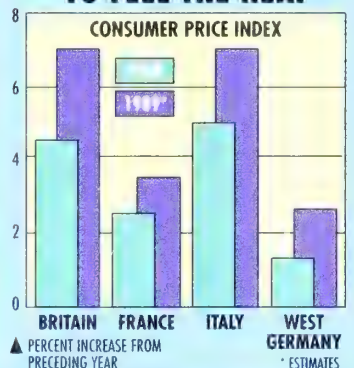
For the past two years, Europe's economy has performed brilliantly. But the consumer and investment boom that has kept factories working at capacity is now producing a worrisome bout of inflation. Higher prices and even a wage-price spiral in some countries threaten to unravel the hard-won gains.

As in the U.S., interest rates are going up across Europe in an attempt to smother price hikes, but the rate increases may be lagging behind the new inflation fears of business and consumers. The standard forecasts are for inflation in the European Community to rise to 4.5%, up a full percentage point from last year. The hardest-hit nations, such as Britain and Italy, will be in the 7% range, and with inflationary expectations on the rise, some corporate leaders see further interest rate increases. "I think that if rate hikes succeed in curbing inflation, they will be welcome," says Jean-Louis Beffa, chairman of Saint-Gobain, the leading French glass and packaging group.

PACESETTER. But so far, European monetary authorities have not had any more luck than the U.S. Federal Reserve in cooling overheating economies. "All of us in Europe are going to be completely windied if we keep going at this rate," warns Carlo Andrea Bollino, chief economist at ENI, Italy's state-owned oil company. "The problem is that in slowing down, are we going to get a chance to catch our breath, or are we going to get a full-blown recession?"

As the interest-rate pacesetter, West Germany's Bundesbank has reacted strongly, triggering increases across Europe. With prices in Germany rising at a 2.6% annual clip, twice as fast as last year, Germany's central bankers have

THE CONSUMER STARTS TO FEEL THE HEAT



its earlier rate increases to take hold.

But with German factories running at full tilt, more price increases are coming. Strong orders for German machinery have factories working at 89.2% of capacity, the highest level in 15 years. As a result, even the inflation-fearing Germans are beginning to make price increases stick. Auto maker BMW, for example, pushed up car prices across its

pushed interest rates up by more than two points since November. A recent strengthening of the mark against the dollar has temporarily calmed the anti-inflationary zeal of the bank, which now seems willing to allow some time for

model range an average of 2.5% on Feb. 13. Given such trends, the Bundesbank will almost certainly have to hike rates by at least another quarter to half a point, lifting the key Lombard rate to 6.25% or 6.5%. Most other European central banks are expected to follow suit. Only in Britain, where monetary authorities have sent rates to a punishing 13%, have retail sales and consumer borrowing started to slow. Elsewhere, consumers are still on a spree. In January sales of French auto maker Peugeot increased by 22.5%. February was another strong month, and some company officials have begun to wonder if projections of a 3% decline in European auto sales in 1989 will materialize.

Corporations are in much better shape to handle interest-rate increases now than they were in the last inflation bout



years ago. With profits up, many European companies have spare cash and can self-finance much of their capital projects. Some are even paying down their loans. The Swedish telecommunications group L. M. Ericsson has retired most of its short-term debt and converted \$1.3 billion in long-term loans to fixed rates. "We are exceptionally well prepared for higher rates," says Carl-Wilhelm Ros, executive vice-president for finance.

WAGE PRESSURES. In Italy, there's no sign yet that higher rates are slowing lending. On March 3 the Italian central bank raised the discount rate by a full point, to 13.5%. By keeping the lira strong, higher interest rates are contributing to the deterioration of Italy's trade balance, now sinking into the red at an unprecedented rate. Says Bruno Lamorgghini, a vice-president at computer maker Olivetti: "Our international competitiveness is getting more and more problematic because of the overvaluation of the lira."

Wage pressures in such countries as Italy and Britain also augur badly for the European outlook. With Britain's inflation up from 4.5% to 7.5% since early last summer, unions are aggressively pushing for double-digit settlements. Annual wage increases for British factory workers averaged 6.9% in last year's fourth quarter. Companies such as Ford Europe Inc. that have labor contracts linked to consumer prices are also being squeezed hard. Ford's British workers recently got an 8.9% pay hike.

In Britain, and on the Continent, productivity gains won't keep up with such hefty wage hikes, and analysts are now concerned that the British may be about to set off a damaging wage-price spiral. "In the present climate of inflation and high interest rates is not great for business," says Henry A. Sweetbaum, chairman of Wickes PLC, a \$1.2 billion retailer of home-improvement supplies. He's getting higher wage demands just as sales have become erratic.

Once inflationary expectations take hold, in fact, it becomes doubly hard to hold down wage gains, even if orders begin to sag. European central bankers are finding they have to apply the brakes harder and harder to obtain results. Although the West German central bank did not follow the recent increase in the discount rate in the U.S., the Bundesbank has left financial markets and executives on edge. For now, the prospect of an interest-rate war with the U.S. is diminished. The current period of calm is likely to be temporary, however. Price pressures mean interest rates have only one way to go. Up.

By Blanca Riemer in Paris, with Mark Tremont in London, John Templeman in Bonn, and bureau reports

JAPAN

THE RECRUIT SCANDAL BUBBLES TO THE TOP

A furor over favors could drag down both Nakasone and Takeshita

It was a sorry end to one of the most illustrious careers in Japanese industry. In December, Hisashi Shinto was forced to resign as chairman of giant Nippon Telegraph & Telephone Corp. because of links to the Recruit Co. stock scandal. His home besieged by reporters, Shinto, 78, moved from hotel to hotel and finally to a hospital. On Mar. 6 he moved again. As a stunned Japan looked on, prosecutors arrested Shinto, took him to a criminal-detention center, and charged him with accepting bribes from Recruit.

Nine months after breaking open, the Recruit scandal has suddenly reached Lockheed-like proportions. It is being pursued by the same aggressive prosecutors as broke the Lockheed case. In 1976 former Prime Minister Kakuei Tanaka was indicted for taking a bribe from Lockheed Corp. Shinto's arrest is putting similar heat on Yasuhiro Nakasone, who was Prime Minister at the time of the alleged Recruit bribery and is still a powerful figure within the ruling Liberal Democratic Party. "Everyone expects Nakasone will be next," says political scientist Hajime Shinohara. The Recruit scandal also could force Prime Minister Noboru Takeshita to resign before his term ends next fall.

STOCK SWAP? It has been known for months that Recruit, a young company, sought influence in high places by selling cheap shares in a real-estate subsidiary, Recruit Cosmos, to 160 top politicians, bureaucrats, and business leaders. The stock was mostly placed with aides or relatives. Aides to Shinto, Nakasone, and Takeshita made big profits when the stock went public in 1986. About \$70,000 ended up in Shinto's own bank account.

What prosecutors appear to be zeroing in on now is the possibility that Nakasone and Shinto repaid the favor by helping the information-services company obtain two Cray Research Inc. super-

computers. Opposition parties claim that Nakasone orchestrated the deal. At a meeting with President Reagan in Washington in May, 1987, the then-Prime Minister discussed the need for Japan to buy U.S. supercomputers, then a hot trade issue. Nakasone told Reagan that NTT planned to buy one. When Cray sold two supercomputers to NTT, the phone company resold them to Recruit, allegedly at a special price. Thus there may have been a back-scratching deal. There is no hint Cray engaged in questionable dealings.

WEAKENED GRIP. Nakasone's control of his own LDP faction is already starting to slip. At a Feb. 27 press conference he denied any wrongdoing. But his effort to quiet the furor backfired, forcing him to cancel a U.S. trip. As the clouds gather over him, several prominent faction members are jockeying for position.

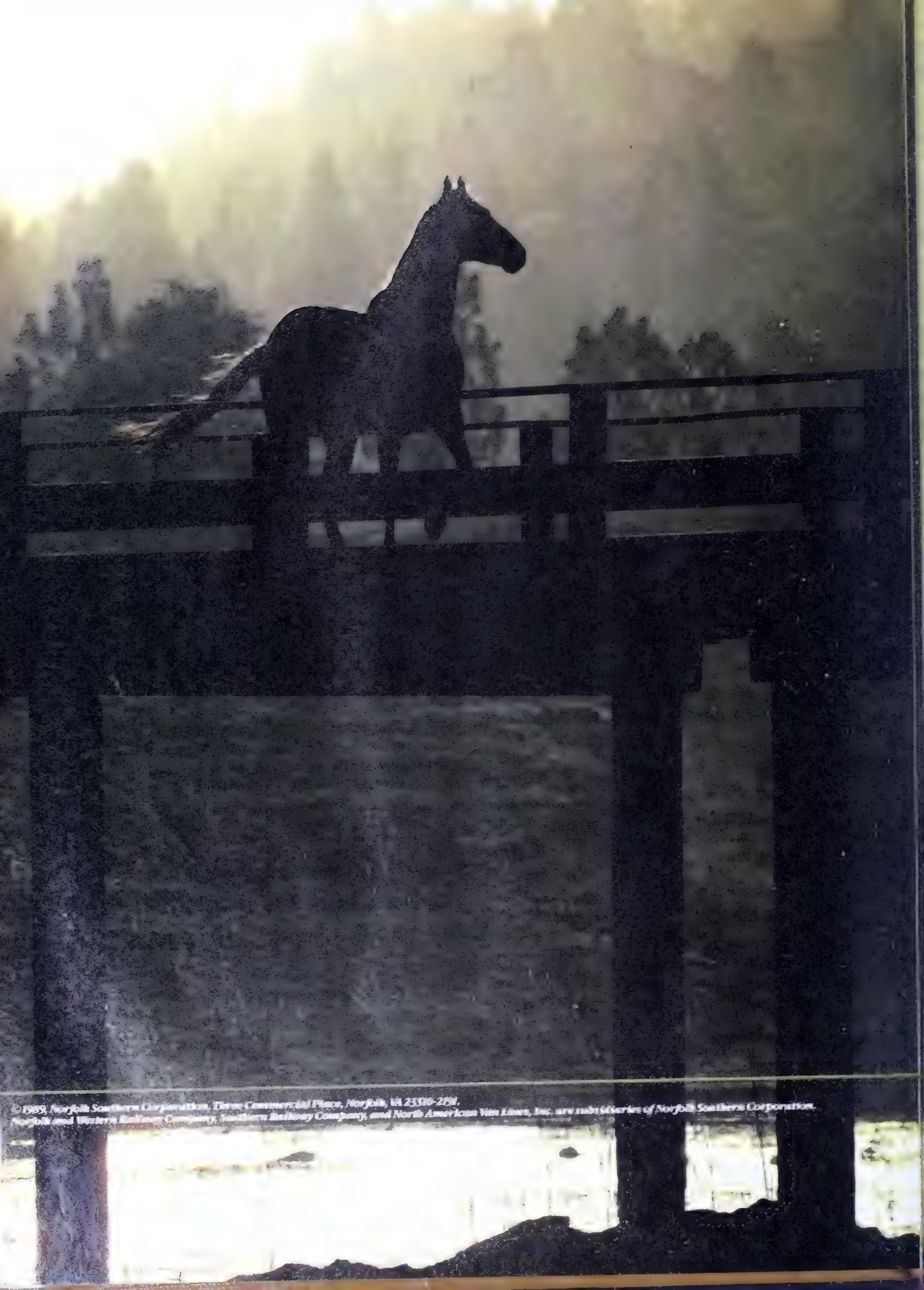
Shinto's arrest also has already weakened Takeshita's grip on the Diet and party affairs. On Mar. 8, Japan's opposition boycotted a key parliamentary budget committee in an attempt to force Nakasone to testify about Recruit. But if Takeshita makes Nakasone testify, he risks the wrath of the former premier's LDP followers. Diet members have begun to wonder whether Takeshita can hang on. The prosecutors' decision to arrest Shinto, although his aide alone bought the stock, could even pave the way for action against Takeshita himself.

NTT won't be able to shake the Recruit affair easily either. Local authorities in Tokyo and other cities recently banned NTT from bidding on some telecommunications projects. The arrests of Shinto and three other former NTT officials have revived calls for the phone company to be broken up. For Shinto, the gruff former shipbuilding executive who guided NTT through privatization, that would be the final humiliation.

By Amy Borrus in Tokyo



Nakasone: Did he
repay Recruit with
a discount
computer deal?



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WASHINGTON'S NEW, SOFTER LINE ON LATIN DEBT

The Brady plan offers incentives to banks to write down their loans



VENEZUELAN RIOTED TO PROTEST STRINGENT ECONOMIC REFORMS

Treasury Secretary Nicholas F. Brady is leading the Bush Administration into an about-face on Third World debt, Washington's first policy reversal on the issue since 1985. Shaken by riots in Venezuela last month after President Carlos Andrés Pérez imposed stringent economic reforms, Brady will endorse efforts by big borrowers to reduce their debt load.

Apparently acting in concert with Japan's Finance Ministry, Brady will suggest—perhaps as early as Mar. 10—that commercial banks voluntarily write down loans, offer debtors lower interest rates, and extend the terms of remaining credits to countries that have reformed their economies. To persuade skeptical bankers to sign on to the plan, Brady will offer as-yet-unspecified financial incentives, perhaps including World Bank guarantees and new Japanese financing, to assure the banks that they will collect their renegotiated loans. In early March, Assistant Treasury Secretary Charles H. Dallara met with senior Finance Ministry officials in Tokyo to sell the Brady plan and, perhaps, work out financing details.

A 'WINDOW.' The U.S. and its allies may even establish a special financial assistance "window" at the International Monetary Fund to help debtors buy back existing debt at a discount. The facility,

similar to one set up in 1974 to help countries with OPEC-induced balance-of-payments problems, may be funded by Japan, with a 50% share, European nations, which would provide 30% of any funds, and the U.S., which would pick up the remainder.

Latin debtors have been seeking debt relief for years. But even before word of the Brady plan leaked out, many bankers were coming around to the notion that Latin America's mounting political stresses make reductions inevitable. Since 1987 big U.S. banks have set aside reserves to cover 25% to 35% of their Third World exposure. While they have been using the reserves to cover write-downs, some bankers say they might pick up the pace if Washington provided them with an incentive. "It would be nice to see a fresh, new scheme," says one New York banker. But he adds: "There are lots of problems. As part of the new approach, economic adjustments will have to take place in the debtor countries."

The plan's emphasis is far different from the \$20 billion in new bank lending envisioned by James A. Baker III, now Secretary of State, when he crafted the

Reagan Administration's policy in 1983. And even before it is fully formed, Brady's proposal is facing objections from Congress, the State Dept., and the Federal Reserve Board.

Some government hardliners are already questioning whether the plan's financial incentives will ultimately shift the Latin debt burden from banks to the U.S. taxpayer. And the Fed, one of the few agencies consulted by Treasury during the review, objects that banks under pressure to make concessions on old debt won't be willing to lend new money to Latin American countries, cutting off the flow of funds needed for investment. **'NO ANSWER.'** Nor has Treasury outlined how it will ensure that debtor nations keep up reforms. Such objections "are the things that Treasury used to talk about as reasons not to change the strategy," says a government source. "Now when you ask these questions, there's no answer."

Debtors and congressional critics worry the plan doesn't go far enough. "I've urged them to err on the side of boldness—the days of gradualism are over," says Representative Jim Leach (R-Iowa), a senior member of the Banking Committee. But for debtors, "the only relevant question is how much of a write off there will be," says Luis Paulo Rosenberg, a former adviser to Brazilian President José Sarney. Under the plan proposed by Brady, the answer still remains



BRADY MAY APPROACH SKEPTICAL BANKERS AS EARLY AS MAR. 10

Only as much as banks will accept.

But banks may be willing to accept more than they have to date. A new international banking regulation scheduled to take effect in 1992 will limit banks' ability to count their Third World loan-loss reserves as capital. That alone may encourage banks to recognize losses sooner, perhaps writing down their portfolios by 25% or more. Even that may not be enough. One European banker now values Mexican debt at only 24¢ on the dollar, implying a 76% write off would be more in order.

Still, the Venezuelan crisis has concentrated minds at the Treasury Dept. The Brady plan, developed at the leisurely pace of George Bush's Washington, isn't complete yet. It likely will be some weeks before it becomes clear whether Brady's approach can fly.

By Mike McNamee in Washington, with Jeffrey Ryser in Sao Paulo and Leah Nathans in New York

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THE VOICE OF ARGENTINE VOTERS WILL ECHO THROUGH LATIN AMERICA

Argentina gave Latin American democracy a boost in 1983 by electing Raúl Alfonsín as President with a mandate to consolidate constitutional rule after decades of political turmoil. Next December, Alfonsín will be the first elected President to hand over power to an elected successor in Argentina since 1928. And Argentine voters may set another important example when they choose that successor in elections on May 14. That will mark the first major Latin American election after riots in Venezuela against austerity measures imposed by President Carlos Andrés Pérez. So the outcome will be an important barometer of popular sentiment in the debt-laden region.

Front-runner Carlos S. Menem, 56, the Peronist governor of La Rioja province, is a free spender who is unlikely to take the hard steps needed to revitalize Argentina's stagnant economy and get foreign creditors' help in restructuring its \$59 billion debt. The flamboyant, bewhiskered Menem, who likes to be photographed hugging chorus girls and in other unconventional poses, aims to build a following based on personal loyalty rather than policies or ideology. He follows the tradition of Latin *caudillos*, or populist strongmen, such as former President Juan D. Perón.

CONTRADICTIONARY. As the presidential candidate of the opposition Justicialist Party, the Peronist movement's formal name, Menem attracts voters who blame Alfonsín and his Radical Civic Union party for falling living standards. Although Alfonsín is widely respected for strengthening Argentine democracy and curbing the military, his economic program failed to slow triple-digit inflation and halt Argentina's economic slide. Admits a government official: "People can't eat democracy."

Nevertheless, Radical Party candidate Eduardo C. Angeloz, 57, the pragmatic governor of Córdoba province, appears to be narrowing Menem's lead to a range of 5% to 10% in current polls, down from 15% to 20% in early February. Compared

with Menem, Angeloz is a colorless campaigner. But he is offering a strategy for modernizing Argentina's protected economy with market-opening steps, spurs to foreign investment, and privatization of such key sectors as communications, energy, and transport.

By contrast, Menem proposes few clear-cut policies and often contradicts himself in bidding for support from key groups. He endorses privatization but has assured right-wing union bosses who support him that state-run businesses will not be cut back. He talks of military reform but has promised the generals a bigger budget. While endorsing deregulation, he promises top industrialists, traditionally dependent on close government ties, that they will not be hurt. Born a Moslem of Syrian immigrant parents, Menem is a convert to Catholicism. He tells the state-supported Church that it will not have to make economic sacrifices and



MENEM IS UNLIKELY TO PREACH AUSTERITY

will have a bigger role in education and social policy.

What worries many Argentines even more is Menem's Peronist heritage. Under Juan Perón and his successor, Isabel Perón, the movement was authoritarian, statist, chauvinist and corrupt—until the army seized power in 1976. Last month in a bid for militant nationalist support, Menem seemed to call for a new military grab for the British-ruled Falkland Islands—then backed down after stirring a public outcry.

Argentines who take their cue from the rioters in Venezuela are likely to vote for Menem. More likely to support Angeloz are those who heed Pérez' admonition to his countrymen: The primary responsibility for Latin economic problems lies at home, not with foreign creditors. If Argentines translate that message into votes on May 14, their example could encourage difficult steps toward recovery in the rest of Latin America as well.

By Richard Kessler in Buenos Aires and Jeffrey Ryser in Sao Paulo

GLOBAL WRAPUP

TIBET

China's decades-long delay in fulfilling its promise of autonomy for Tibet is fueling increasingly fierce opposition to its rule. Led by Tibetan nationalists, rioters in the capital of Lhasa challenged Chinese rule in early March, leaving 15 dead and 110 injured. The riots may be a sign that the authority of the Dalai Lama, the moderate religious leader and head of Tibet's India-based government-in-exile, is eroding—and with it, his ability to restrain more radical nationalists. The militant Tibetan Youth Congress is calling for violent resistance to the Chinese, and there are reports of Tibetan

terrorist groups, some hidden in Buddhist monasteries.

The riots erupted on the 30th anniversary of an uprising in which the Chinese killed thousands of Tibetans. Although the casualties were much smaller this time, they are likely to draw attention to China's human rights abuses. That issue strained relations with the U.S. during President Bush's recent visit to Beijing.

China pledged extensive self-rule for Tibet after occupying it militarily in 1951. In a speech last year, the Dalai Lama proposed a political settlement in which Tibet would give up its long-standing demand for full independence in exchange for the right to internal

self-determination. The alternative, he told hardline Tibetan nationalists, would be cultural extinction. But Beijing has been slow to respond and has quibbled over the mechanics of the negotiations. And the death in January of the Beijing-based Panchen Lama, Tibet's second-ranking religious leader, deprived both sides of a valuable intermediary.

If Beijing fails to make good on its promise in Tibet, it risks stirring up new anxieties about Chinese intentions among the residents of Hong Kong. The Colony will become part of China in 1997 under a guarantee of self-rule that is similar to Beijing's assurances to Tibet.

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THE BOTTOM LINES ARE

BUT THE BEARS ARE SHOWING THEIR TEETH AS INDICATIONS OF A SHARP SLOWDOWN

Robust 1987 corporate earnings couldn't keep the bears away a year ago, after Bloody Monday took the fun out of the sixth year of economic expansion. Economists feared a slowdown—even a recession—some time in 1988.

They couldn't have been more wrong. Instead of crashing, the economy continued its deliberate advance. Corporate profits soared. The 900 companies in *BUSINESS WEEK*'s 1988 Corporate Scoreboard, which is compiled by Standard & Poor's Compustat Services Inc., notched a 31% increase in earnings for the year on an 11% rise in sales. Fourth-quarter profits surged 28%, marking the sixth straight double-digit quarterly increase.

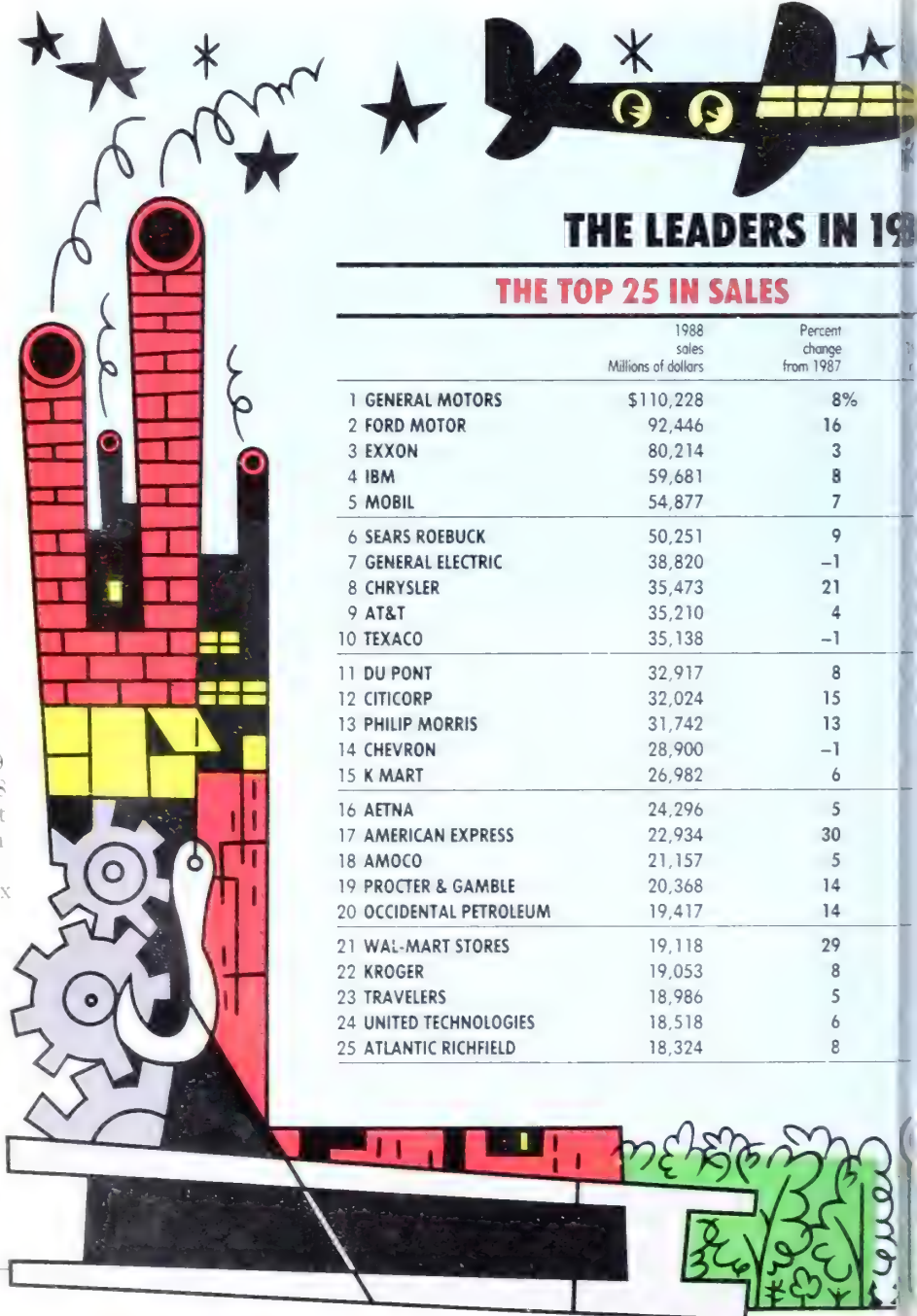
The bears haven't left, though. Now they're citing evidence that go-go profit growth is over. And this time their case looks stronger. Pinched industrial capacity is raising prices. Wages are inching higher while productivity marks time. Fearing inflation, the Federal Reserve is already pushing interest rates up. Says Abby Joseph Cohen, senior investment strategist at Drexel Burnham Lambert Inc.: "We've had the peak in earnings momentum and margins." Like other analysts, she's predicting that earnings will grow 13% this year, followed by a 20% or so decline in 1990.

TAX BREAKS. To a certain extent, 1989 is competing unfavorably with a 1988 that was pumped up by some potent onetime factors. Christopher Caton, an economist with Data Resources, calculates that changes in the nation's tax laws accounted for almost half of last year's remarkable profit leap by lowering the corporate rate and encouraging companies to defer income into 1988. Big write-downs in 1987 also made last year look better. Banks, for instance, staged the most impressive profit turnaround in the Scoreboard. But that was after rebounding from Third World loan write-offs, which helped drive 1987 results \$4.7 billion into the red.

Even so, fundamental strength

in the economy sparked 1988 profits to their strongest showing since the expansion began in 1982. Last year's percentage increase was double 1987's. Economic growth and a weak dollar kept demand for products high. And companies leaner from a multitude of restruc-

turings were better equipped to take full advantage of their strong markets. Metals companies, such as Aluminum Co. of America and Inland Steel Industries Inc., grew by leaps and bounds, benefiting from rejuvenated operations and strong sales. The weak dollar made for



THE LEADERS IN 1988

THE TOP 25 IN SALES

	1988 sales Millions of dollars	Percent change from 1987
1 GENERAL MOTORS	\$110,228	8%
2 FORD MOTOR	92,446	16
3 EXXON	80,214	3
4 IBM	59,681	8
5 MOBIL	54,877	7
6 SEARS ROEBUCK	50,251	9
7 GENERAL ELECTRIC	38,820	-1
8 CHRYSLER	35,473	21
9 AT&T	35,210	4
10 TEXACO	35,138	-1
11 DU PONT	32,917	8
12 CITICORP	32,024	15
13 PHILIP MORRIS	31,742	13
14 CHEVRON	28,900	-1
15 K MART	26,982	6
16 AETNA	24,296	5
17 AMERICAN EXPRESS	22,934	30
18 AMOCO	21,157	5
19 PROCTER & GAMBLE	20,368	14
20 OCCIDENTAL PETROLEUM	19,417	14
21 WAL-MART STORES	19,118	29
22 KROGER	19,053	8
23 TRAVELERS	18,986	5
24 UNITED TECHNOLOGIES	18,518	6
25 ATLANTIC RICHFIELD	18,324	8

TILL GLOWING

YEAR AND IN 1990 GROW STRONGER

foreign imports expensive, and with mills running full tilt, average steel and aluminum prices rose sharply, further fueling earnings.

Other leaders in profit growth also benefited from price hikes. Chemical, paper, and paper container companies

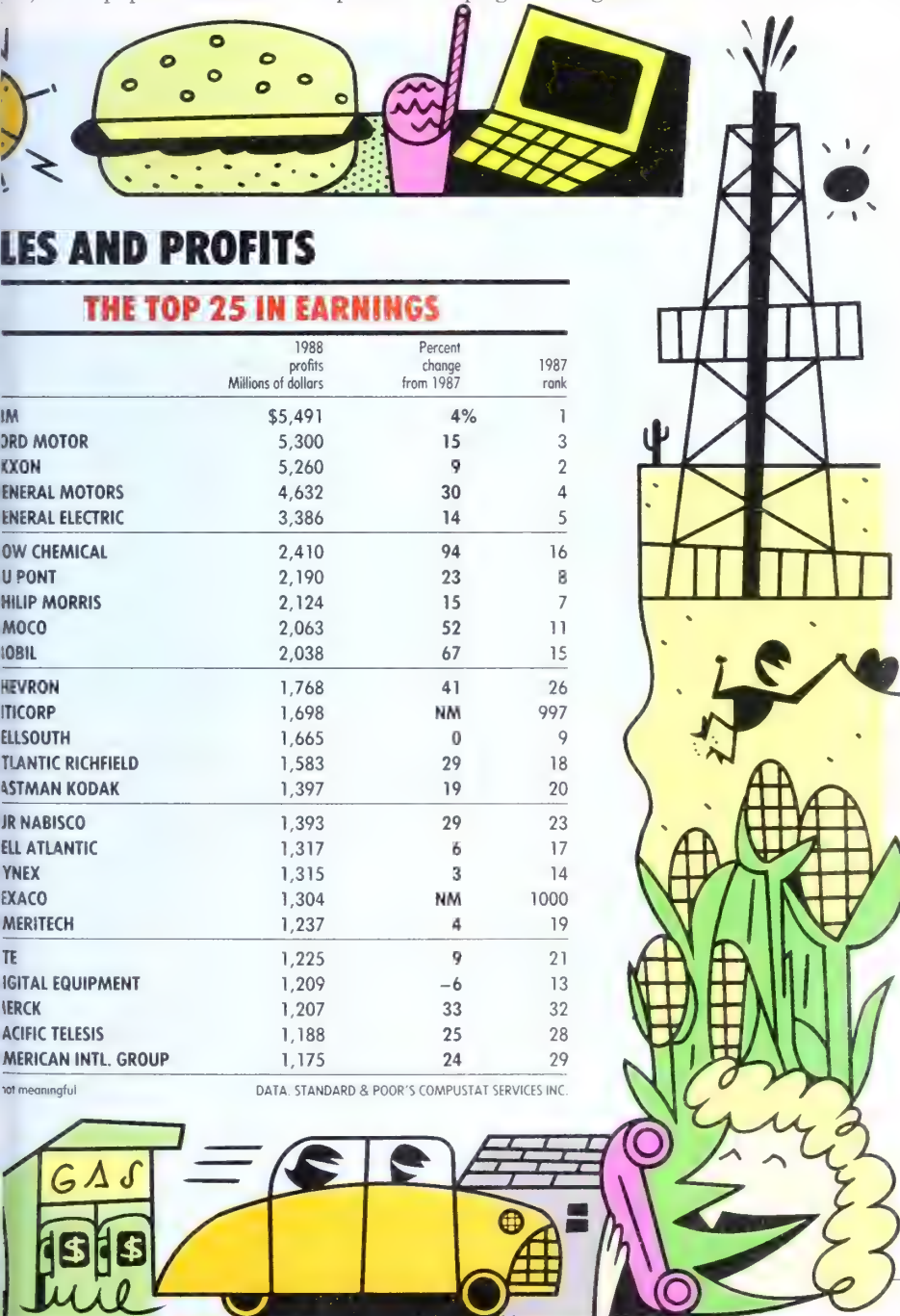
surged to the top of the earnings chart as margins increased sharply. But in the oil patch, it was low crude prices that lifted profits. As oil prices fell, refining margins rose. That was enough to offset severely depressed production margins, helping the oil giants bounce back from

a 1987 profit season that was marred by Texaco Inc.'s \$4.8 billion write-off of its settlement with Pennzoil Co. Meanwhile, in the petroleum services business, earnings at Dresser Industries Inc. took a giant leap of 653% as huge payroll reductions and a big petrochemical acquisition began to pay off. That lifted a sector otherwise characterized by mixed fortunes.

Machinery manufacturers also gained as new operations and closer attention to efficiency began to pay dividends in the expansion. A retooled Harnischfeger Industries Inc. increased profits 150% as sales of its papermaking machinery surged 42%. Both Cincinnati Milacron Inc. and Clark Equipment Co. rebounded from big 1987 write-offs to post strong gains last year.

In many cases, the expanding economy pumped up profits simply by putting more customers in a buying mood. Ford Motor Co. used a 6.5% rise in worldwide vehicle sales to pass Exxon Corp. as Corporate America's second-largest generator of both sales and earnings (table). General Motors Corp. kept the sales lead, while IBM reigned in profits. Even the airlines, which boosted ticket prices substantially last year, attracted more customers. As revenue passenger miles jumped 4.4%, airline profits soared—with the notable exceptions of troubled Texas Air Corp. and Pan Am Corp.

The rising tide didn't lift everyone's boat. The auto parts sector suffered as Eagle-Picher Industries Inc. set aside \$560 million to cover potential asbestos liabilities. Retailing giant Sears, Roebuck & Co. dropped from 10th place on the profits list to 33rd as earnings skidded 40%. And while nuclear construction write-offs and warm winter weather plagued utility profits, an otherwise bright picture in telecommunications was dwarfed by American Telephone & Telegraph Co.'s \$3.9 billion fourth-quarter write-off to retire old equipment. A sluggish building environment hurt the housing and real estate market, but a \$288 million loss at



LES AND PROFITS

THE TOP 25 IN EARNINGS

	1988 profits Millions of dollars	Percent change from 1987	1987 rank
IBM	\$5,491	4%	1
FORD MOTOR	5,300	15	3
EXXON	5,260	9	2
GENERAL MOTORS	4,632	30	4
GENERAL ELECTRIC	3,386	14	5
DOW CHEMICAL	2,410	94	16
PONTIAC	2,190	23	8
PHILIP MORRIS	2,124	15	7
COCA-COLA	2,063	52	11
AMMOBIL	2,038	67	15
HEVRON	1,768	41	26
INTERNATIONAL CORP.	1,698	NM	997
WELLSOUTH	1,665	0	9
ATLANTIC RICHFIELD	1,583	29	18
WESTMAN KODAK	1,397	19	20
JOHN NABISCO	1,393	29	23
WELLS ATLANTIC	1,317	6	17
LYNEX	1,315	3	14
EXACO	1,304	NM	1000
MERITECH	1,237	4	19
TELE	1,225	9	21
DIGITAL EQUIPMENT	1,209	-6	13
VERECK	1,207	33	32
PACIFIC TELESIS	1,188	25	28
AMERICAN INTL. GROUP	1,175	24	29

not meaningful

DATA: STANDARD & POOR'S COMPUSTAT SERVICES INC.

CORPORATE SCOREBOARD

Southmark Corp., because of dubious management of a huge junk bond portfolio, hurt the sector's profits more. Speaking of mismanagement, savings and loan profits slid 14%.

Even the best managers seem to be in for a harder time this year. "The environment won't be hospitable to a rapid growth in earnings," says Morgan Stanley & Co. economist Stephen S. Roach. Already, the price hikes that benefited so many of this year's Scoreboard lead-

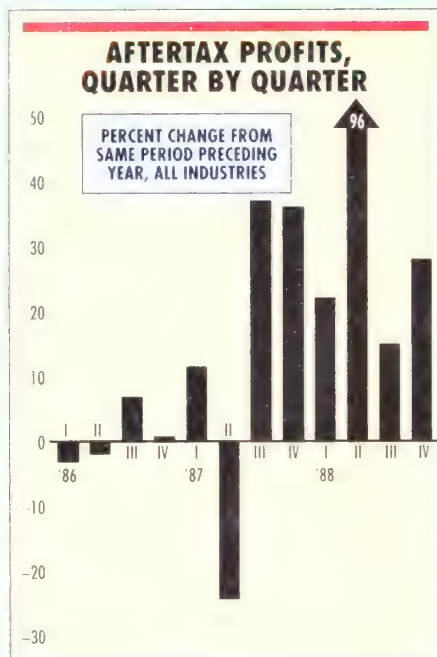
ers are putting pressure on others farther up the line. Witness Caterpillar Inc., typical of companies that surged in 1988. The rehabilitated construction equipment maker rode the export boom to a 93% gain in earnings last year. But rising raw materials prices and a new labor agreement slowed fourth-quarter profits. At Goodyear Tire & Rubber Co. rising rubber prices helped deflate year-end profits by 32%.

There's no quick solution: In this ex-

pansion, capital spending has focused on refurbishing old plants rather than building new ones. That means expanding capacity in key industries is likely to take some time, keeping pressure on prices. Economists and Wall Streeters alike hope that leaner, stronger companies will land more softly in the next downturn. But after a seven-year march there's little question that the slowdown is already in sight.

By Michael Oneal in New York

A SPOTLIGHT ON 1988 INDUSTRY PROFITS



INDUSTRIES WITH THE BIGGEST DOLLAR CHANGE IN 1988

Chalk up six quarters in a row with double-digit gains. Profits soared 31% in 1988, and these industry groups had the biggest impact on a \$44.2 billion increase

EASTERN BANKS

OIL & GAS

WEST & SOUTHWEST BANKS

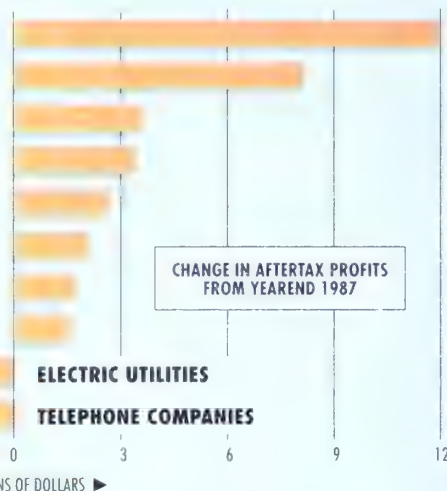
CHEMICALS

MIDWESTERN BANKS

MEDICAL PRODUCTS

CARS & TRUCKS

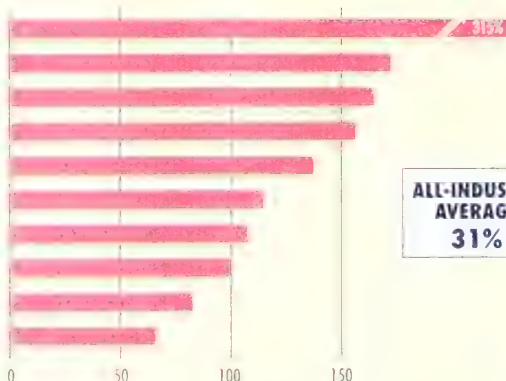
ALUMINUM



WINNERS AND LOSERS IN THE YEAR'S PROFIT RACE

THE STAR PERFORMERS...

ALUMINUM
PETROLEUM SERVICES
MACHINE, HAND TOOLS
MEDICAL PRODUCTS
TELECOMM. SERVICES
STEEL
OIL & GAS
SPECIAL MACHINERY
BROADCASTING
PAPER CONTAINERS



ALL-INDUSTRY AVERAGE
31%

Banks, airlines, and coal — losers in 1987 — were in the black in 1988, but percentage increases in profits can't be calculated meaningfully

...AND THE LAGGARDS

GAS & TRANSMISSION
CONGLOMERATES
ELECTRIC UTILITIES
TRANSPORTATION SERVICES
SAVINGS & LOAN
FOOD RETAILING
TELEPHONE COMPANIES
GLASS CONTAINERS
TIRE & RUBBER
AUTO PARTS & EQUIPMENT

In addition, instruments, construction services, and real estate all reported losses for the full year 1988

DATA: STANDARD & POOR'S COMPUSTAT SERVICES INC.

CORPORATE SCOREBOARD

FOURTH QUARTER 1988

GLOSSARY

Sales: Includes all sales and other operating revenues. For banks, includes all operating revenues.

Profits: Net income before extraordinary items. For banks, profits are net income after currency gains or losses.

Margins: Net income from continuing operations before extraordinary items as percent of sales.

Return on common equity: Ratio of net income available for common stockholders (most recent 12 months) to latest available common equity, which includes common stock, capital surplus, and retained earnings.

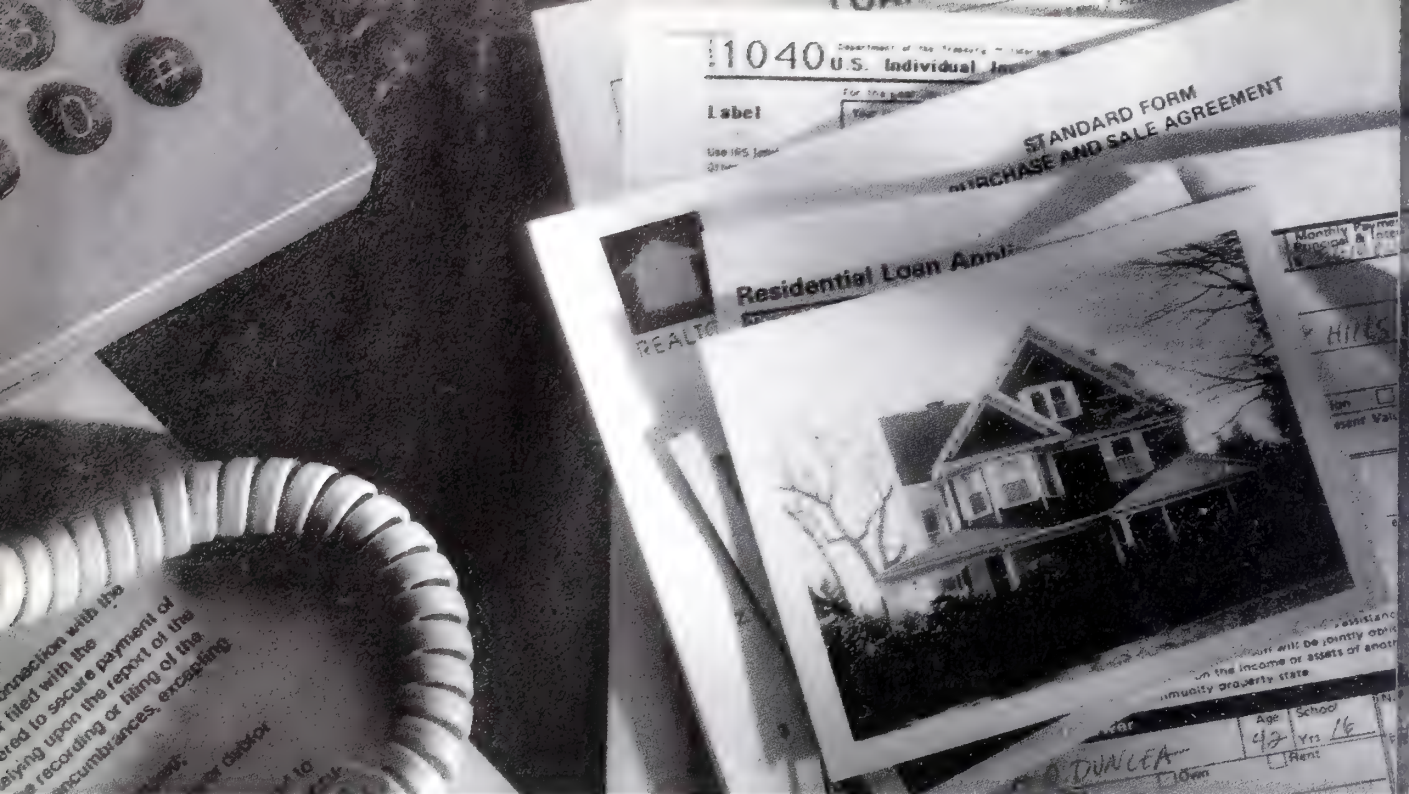
Price-earnings ratio: Based on Feb. 28, 1989, common stock price and corporate earnings from continuing operations before extraordinary items for most recent 12-month period.

Earnings per share: For most recent 12-month period. Includes all common-stock equivalents.

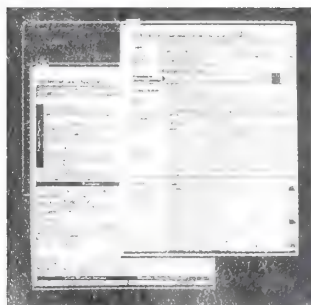
COMPANY	SALES				PROFITS				MARGINS			RETURN ON COMMON EQUITY 12 MONTHS ENDING 12/31	PRICE- EARNINGS RATIO 2/28	12 MONTHS' EARNINGS PER SHARE
	4th QUARTER 1988 \$ MIL	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL	CHANGE FROM 1987 %	4th QUARTER 1988 \$ MIL	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL	CHANGE FROM 1987 %	4th QUARTER 1988 %	4th QUARTER 1987 %				
ALL-INDUSTRY COMPOSITE	890821	10	3354747	11	42227	28	185393	31	4.7	4.0	14.8	12	3.05	
AEROSPACE														
INDUSTRY COMPOSITE	26237.9	7	93328.1	6	670.6	-11	3132.3	12	2.6	3.1	13.4	10	4.53	
Boeing	4872.0	5	16962.0	9	174.0	23	614.0	28	3.6	3.0	11.6	15	4.02	
GenCorp ⁽¹⁾	531.0	18	1891.0	17	5.0	-69	55.0	206	0.9	3.5	NM	10	1.72	
General Dynamics	2490.2	2	9551.0	1	110.2	16	379.0	-13	4.4	3.9	20.7	6	9.03	
Grumman	1035.7**	9	3648.9	8	24.1	NM	86.5	220	2.3	NM	10.7	8	2.50	
Kaman	191.7	2	767.9	9	4.9	-24	25.3	5	2.5	3.4	14.5	9	1.42	
Lockheed	2983.0	-6	10590.0	-6	104.0	-22	442.0	4	3.5	4.2	18.5	7	7.34	
Martin Marietta	1535.1	16	5727.5	11	23.7	-60	319.8	39	1.5	4.5	26.6	7	6.02	
McDonnell Douglas	4344.0	19	15072.0	10	145.0	56	350.0	12	3.3	2.5	11.5	10	9.13	
Northrop	1726.0	-2	5797.1	-4	-86.1	NM	104.2	11	NM	2.0	-2.8	13	2.22	
Parker Hannifin ⁽⁶⁾	612.6	11	2397.3	15	25.2	3	108.4	19	4.1	4.4	12.4	13	2.24	
Rohr Industries ⁽⁵⁾	224.9	11	928.6	31	7.8	9	33.1	31	3.5	3.5	8.7	17	1.90	
Sundstrand	420.2	11	1477.3	8	-17.9	NM	-44.1	NM	NM	NM	-7.7	NM	-2.39	
United Technologies	5271.5**	9	18517.9	6	150.6	-13	659.1	11	2.9	3.6	14.1	9	5.05	
AUTOMOTIVE														
INDUSTRY COMPOSITE	75127.0	12	286932.1	13	2821.6	15	12153.7	10	3.8	3.6	16.3	6	6.26	
CARS & TRUCKS GROUP COMPOSITE	65149.0	12	248249.7	13	3125.6	42	11480.9	18	4.8	3.8	17.4	5	8.39	
Amerco ⁽⁹⁾	183.3	3	808.5	4	-3.2	NM	38.9	438	NM	0.7	9.0	NA	399.31	
Chrysler	9690.0	14	35472.7	21	433.6	24	1050.2	-19	4.5	4.1	14.4	6	4.66	
Ford Motor	23912.0	14	92445.5	16	1157.9	24	5300.2	15	4.8	4.4	24.6	5	10.96	
General Motors	28849.9	9	110228.5	8	1398.3	67	4632.1	30	4.8	3.2	13.4	6	14.34	
Mack Trucks	544.7	13	2102.2	13	10.3	NM	24.9	407	1.9	NM	4.9	16	0.84	
Navistar International ⁽²⁾	1127.0	13	4080.2	16	82.3	51	258.8	77	7.3	5.4	37.9	7	0.89	
Paccar	842.2	26	3112.2	28	46.4	31	175.8	56	5.5	5.3	19.3	9	4.90	
PARTS & EQUIPMENT GROUP COMPOSITE	6814.6	12	26556.8	13	-373.0	NM	264.2	-63	NM	1.9	3.7	48	0.49	
Arvin Industries	328.8	6	1313.3	0	6.1	-37	16.5	-65	1.9	3.1	3.6	33	0.70	
Champion Spark Plug	183.9	0	738.0	3	7.6	124	22.1	36	4.1	1.8	6.6	35	0.63	
Cummins Engine	869.2	15	3310.1	20	-55.0	NM	-63.4	NM	NM	NM	-11.4	NM	-6.71	
Dana	1237.3	14	4935.7	18	43.7	115	162.2	28	3.5	1.9	17.2	10	3.99	
Danaher	177.7**	3	715.7	16	9.5	43	40.0	96	5.4	3.9	27.4	8	1.68	
Eagle-Picher Industries ⁽¹⁾	202.9	12	770.1	14	-496.4	NM	-465.8	NM	NM	6.4	NM	NM	-43.54	
Eaton	890.9	11	3468.5	11	50.2	14	227.7	10	5.6	5.5	21.1	10	6.11	
Echlin ⁽⁴⁾	356.0	18	1347.8	17	15.2	22	64.8	39	4.3	4.1	10.1	13	1.17	
Federal-Mogul	268.1	0	1176.9	9	9.3	-28	43.4	6	3.5	4.9	12.4	15	3.47	
Fruehauf	557.0	21	2094.4	7	-10.2	NM	-56.5	NM	NM	NM	NM	NM	-6.40	
Masco Industries	402.8	2	1651.5	12	-1.9	NM	82.1	82	NM	NM	22.5	11	0.90	
Pep Boys-Manny, Moe & Jack ⁽¹¹⁾	172.9	21	630.4	17	10.1	24	36.0	5	5.8	5.8	13.5	20	0.65	
Smith (A. O.)	262.3	11	1015.4	5	6.4	217	19.0	23	2.4	0.9	5.3	12	1.86	
SPX	226.1	12	877.7	13	9.7	NM	44.9	72	4.3	NM	14.4	10	3.64	
Sudbury ⁽⁷⁾	152.3**	18	592.6	34	-2.4	NM	3.3	-73	NM	2.5	3.7	38	0.19	
Trinova	526.4	14	1918.6	14	25.0	22	87.8	21	4.8	4.4	12.9	12	2.54	

Fourth quarter ending Nov. 30. (2) Fourth quarter ending Oct. 31. (3) First quarter and most recent 12 months ending Dec. 31. (4) First quarter and most recent 12 months ending Nov. (5) First quarter and most recent 12 months ending Oct. 31. (6) Second quarter and most recent 12 months ending Dec. 31. (7) Second quarter and most recent 12 months ending Nov. (8) Second quarter and most recent 12 months ending Oct. 31. (9) Third quarter and most recent 12 months ending Dec. 31. (10) Third quarter and most recent 12 months ending Nov. (11) Third quarter and most recent 12 months ending Oct. 31. * Sales include excise taxes. ** Sales include other income. *** Sales include excise taxes and other income. † Revenues from major subsidiaries not included in sales. ‡ Annual data from April through December 1988. NA=not available. NM=not meaningful.

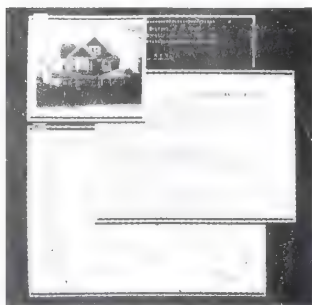
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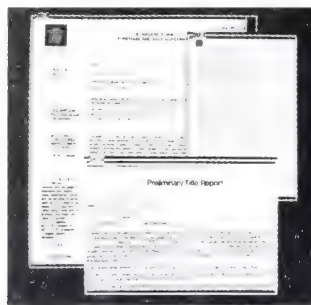
CAN A BETTER IMAGE IMPROVE CUSTOMER SERVICE? BANK ON IT.



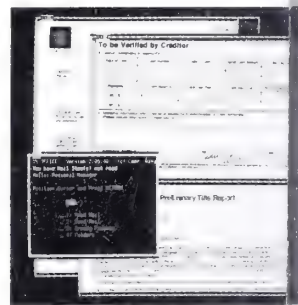
*Customer comes in for a mortgage.
Has a loan application, tax returns.*



*Bank appraiser mails in photos of
property, plot plan and comparables.*

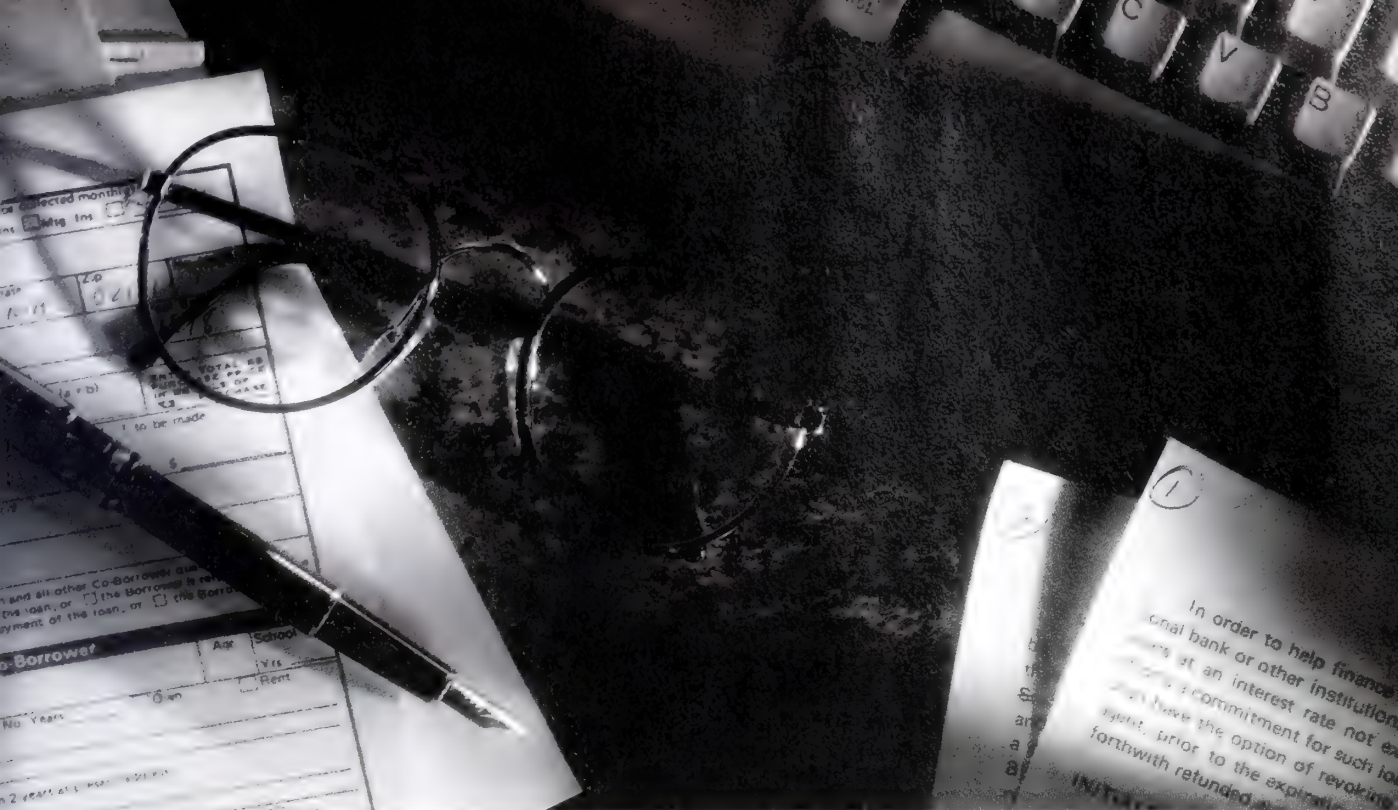


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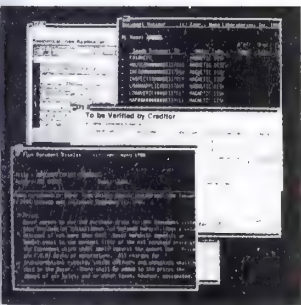
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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE-EARNINGS RATIO 2-28	12 MONTH EARNING PER SHARE	
	4th QUARTER 1988 \$ MIL	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL	CHANGE FROM 1987 %	4th QUARTER 1988 \$ MIL	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL	CHANGE FROM 1987 %	4th QUARTER 1988 %	4th QUARTER 1987 %				
(c) TIRE & RUBBER														
GROUP COMPOSITE	3163.5	8	12125.8	9	69.0	-48	408.5	-27	2.2	4.5	17.2	9	4.76	
Carlisle	141.1	4	567.4	5	-1.3	NM	17.4	-8	NM	3.3	8.9	17	2.16	
Cooper Tire & Rubber	195.2	10	748.0	12	13.9	58	41.1	34	7.1	5.0	16.8	13	2.01	
Goodyear Tire & Rubber	2827.2	8	10810.4	9	56.4	-53	350.1	-32	2.0	4.5	18.0	8	6.11	
3 BANKS														
INDUSTRY COMPOSITE	52093.6	15	189093.1	12	4088.1	108	15019.2	NM	7.8	4.3	16.9	7	4.50	
(a) BANKS - EAST														
GROUP COMPOSITE	30392.5	18	108330.0	15	2601.9	64	8663.2	NM	5.6	6.1	18.7	5	5.62	
Bank of Boston	1461.1	34	5295.6	24	82.7	NM	322.3	NM	5.7	NM	16.4	5	4.66	
Bank of New England	888.2	19	3196.7	19	74.0	487	281.7	104	8.3	1.7	17.3	6	4.06	
Bank of New York	897.0	58	2620.4	22	54.7	19	213.0	106	6.1	8.1	16.5	8	5.61	
Bankers Trust New York	1601.5	-7	5851.3	4	185.5	-35	647.7	NM	11.6	16.5	18.5	5	8.09	
Chase Manhattan	3542.2	27	12364.6	15	275.1	79	1058.9	NM	7.8	5.5	23.9	3	11.55	
Chemical Banking	1991.5	-1	7644.0	13	288.5	26	753.6	NM	14.5	11.4	22.6	3	12.02	
Citicorp	9220.0	22	32024.0	15	587.0	-5	1698.0	NM	6.4	8.2	20.9	5	4.87	
CoreStates Financial	445.8	18	1629.7	12	47.2	11	179.5	11	10.6	11.2	16.2	9	4.50	
Fleet/Norstar Financial Group	811.8	13	3051.1	13	87.6	NM	335.8	68	10.8	1.1	18.9	9	3.07	
KeyCorp	385.1	21	1394.2	19	34.5	293	119.9	65	9.0	2.8	14.2	8	2.90	
Manufacturers Hanover	2255.0	8	8545.0	10	210.0	813	752.0	NM	9.3	1.1	26.6	2	14.24	
Mellon Bank	884.0	-4	3269.0	-2	48.0	NM	-65.0	NM	5.4	NM	-11.9	NM	-3.65	
Midlantic	501.9	23	1846.5	20	59.5	58	222.9	38	11.8	9.2	17.4	7	5.85	
MNC Financial	549.1	21	1983.3	24	49.3	13	170.2	14	9.0	9.6	15.3	8	5.86	
Morgan (J. P.)	2320.0	27	7839.4	15	258.1	15	1001.8	NM	11.1	12.2	17.9	7	5.38	
PNC Financial	1055.7	25	3827.2	21	115.6	255	442.7	73	11.0	3.8	17.5	8	5.09	
Republic New York	591.7	30	2105.1	26	50.0	127	169.6	413	8.5	4.8	13.4	9	5.01	
Shawmut National	716.2	14	2811.2	19	66.1	51	242.6	53	9.2	7.0	15.0	7	3.28	
United Jersey Banks	274.6	14	1032.0	16	28.5	10	116.1	13	10.4	10.8	15.0	9	2.58	
(b) BANKS - MIDWEST														
GROUP COMPOSITE	6854.9	5	26703.6	8	258.8	NM	2210.3	NM	3.8	NM	14.5	9	3.43	
Ameritrust	274.8	12	1052.3	13	26.1	112	103.5	NM	9.5	5.0	14.6	9	2.62	
Banc One	730.4	17	2734.5	15	87.5	28	340.2	47	12.0	11.0	17.2	9	2.61	
Boatmen's Bancshares	354.6	2	1378.2	2	-11.6	NM	69.8	-28	NM	6.2	-1.2	16	2.01	
Comerica	280.7	14	1042.8	11	28.5	17	112.0	57	10.1	9.8	18.3	7	6.78	
Continental Bank	869.3	18	3060.4	10	113.5	NM	315.8	NM	13.1	NM	29.1	4	5.19	
First of America Bank	238.6	15	885.0	15	26.7	15	88.8	13	11.2	11.2	14.7	6	6.16	
First Bank System	164.9	-73	1953.7	-21	-427.3	NM	-310.0	NM	NM	5.9	-36.0	NM	-5.25	
First Chicago	1270.5	5	4815.5	14	137.2	NM	513.1	NM	10.8	NM	26.4	4	8.20	
Manufacturers National	254.2	36	924.4	21	26.3	NM	96.3	NM	10.4	NM	16.8	7	6.40	
National City	611.8	16	2226.7	12	66.5	270	233.2	80	10.9	3.4	17.6	8	3.84	
NBD Bancorp	595.0	17	2180.9	11	61.5	24	227.2	40	10.3	9.7	15.1	8	4.81	
Northern Trust	287.8	27	1003.1	20	42.0	NM	109.3	NM	14.6	NM	27.4	7	6.61	
Norwest	663.7	13	2474.5	8	55.9	20	211.2	NM	8.4	7.9	19.0	8	4.52	
Society	258.8	13	971.6	9	25.9	15	100.1	10	10.0	9.9	14.7	8	4.19	
(c) BANKS - SOUTH & SOUTHEAST														
GROUP COMPOSITE	5649.7	13	21211.3	13	533.1	31	2092.6	33	9.4	8.1	16.1	9	3.21	
Barnett Banks	677.0	13	2545.7	14	59.0	17	226.4	22	8.7	8.4	15.5	9	3.75	
Citizens & Southern	553.5	12	2089.7	13	54.5	10	206.3	31	9.8	10.0	16.7	8	3.25	
Crestar Financial	271.2	9	1016.3	8	22.3	86	86.7	53	8.2	4.8	13.7	9	2.96	
First Union	771.3	14	2899.0	10	70.5	4	296.9	5	9.1	10.0	15.8	8	2.76	
First Wachovia	547.6	15	2020.2	13	62.1	56	244.3	38	11.3	8.4	16.1	9	4.34	
HCNB	748.3	11	2829.8	15	64.3	337	252.5	51	8.6	2.2	13.3	11	2.90	
Signet Banking	322.3	12	1285.8	23	28.3	62	152.5	550	8.8	6.0	23.1	5	5.71	
Southeast Banking	382.3	14	1405.5	10	24.9	2	75.3	222	6.5	7.3	15.8	10	2.35	
Sovran Financial	601.6	9	2230.3	10	68.1	14	243.1	12	11.3	10.9	17.3	8	4.09	
SunTrust Banks	774.5	14	2889.0	13	79.1	11	308.7	9	10.2	10.5	16.8	9	2.38	
(d) BANKS - WEST & SOUTHWEST														
GROUP COMPOSITE	9196.6	16	32849.0	8	694.3	NM	2053.1	NM	7.5	0.4	14.0	8	4.15	
BankAmerica	2993.0	17	10181.0	0	193.0	222	547.0	NM	6.4	2.3	14.2	8	2.77	
First City Bancorp. of Texas	324.7	NA	865.1	NA	25.2	NA	66.1	NA	7.8	NA	11.1	11	2.73	
First Interstate Bancorp	1596.9	23	5932.1	17	117.0	NM	102.4	NM	7.3	NM	4.8	23	2.03	
Security Pacific	2333.1	17	8483.1	11	169.5	NM	638.9	NM	7.3	NM	17.5	7	5.59	
U. S. Bancorp	373.1	16	1380.6	20	34.9	83	123.9	24	9.4	5.9	13.1	9	3.02	
Valley National	300.2	8	1147.4	7	18.7	NM	62.3	NM	6.2	NM	10.1	8	3.16	
Wells Fargo	1275.7	5	4859.7	6	135.9	22	512.5	909	10.7	9.2	22.4	7	9.20	
4 CHEMICALS														
INDUSTRY COMPOSITE	32207.8	12	125399.5	16	2706.6	46	11181.7	42	8.4	6.5	21.1	9	5.60	
Air Products & Chemicals (3)	640.6	9	2486.5	14	61.1	10	219.5	22	9.5	9.4	17.3	11	4.00	
American Cyanamid	1103.1	8	4592.0	10	62.8	4	305.6	16	5.7	5.9	15.4	15	3.41	
Arco Chemical	745.0	47	2700.0	38	134.0	116	494.0	92	18.0	12.2	37.5	6	5.00	
Aristech Chemical	258.5	7	1065.2	16	34.9	63	164.5	136	13.5	8.8	41.3	6	6.66	

Footnotes on page 65



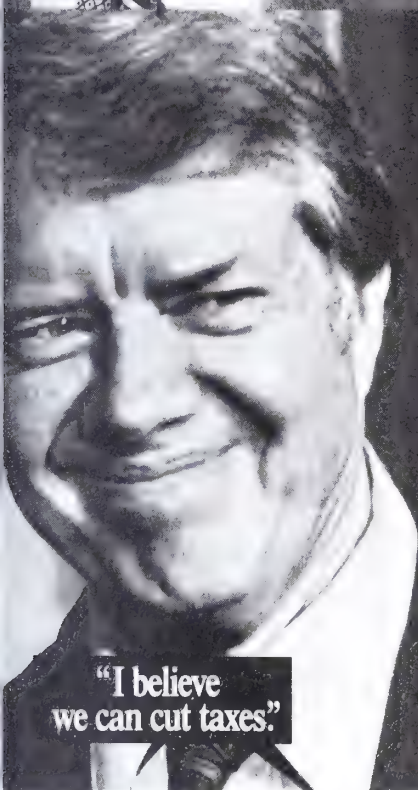
"I am anxious to have taxes reduced."



We're "committed to tax reform."



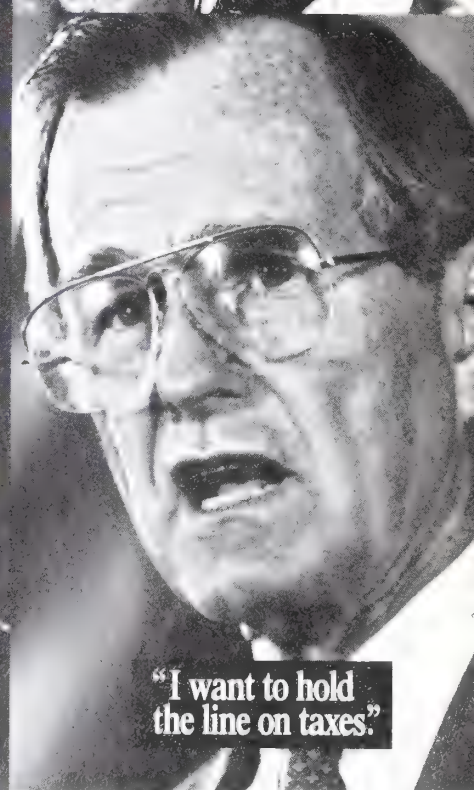
"I stand for lower taxes."



"I believe we can cut taxes."



"I will not raise taxes."



"I want to hold the line on taxes."

WE CREATED TAX-FREE FUNDS. THEN AGAIN, WE HAD A LOT OF INSPIRATION.

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investment income be subject to the ups and downs of economic policy?

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rated tax-exempt fund. Now you don't have to wait and see what happens with taxes in the future. Call us for a prospectus.

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The right fund at the right time.

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12 31	PRICE EARNINGS RATIO 2 28	12 MONTHS EARNING PER SHARE
	4th QUARTER 1988 \$ MIL	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL	CHANGE FROM 1987 %	4th QUARTER 1988 \$ MIL	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL	CHANGE FROM 1987 %	4th QUARTER 1988 %	4th QUARTER 1987 %			
Cabot (3)	480.1	24	1769.9	21	22.8	40	67.7	85	4.7	4.2	11.9	17	2.48
Dexter	205.5**	4	837.3	9	8.6	-25	39.9	-8	4.2	5.8	13.3	21	1.61
Dow Chemical	4299.0	20	16682.0	25	635.0	79	2410.0	94	14.8	9.8	35.1	7	12.82
Du Pont	8441.0	6	32917.0	8	500.0	14	2190.0	23	5.9	5.5	14.5	10	9.11
Engelhard	695.1	-5	2350.7	-5	19.2	52	63.7	-9	2.8	1.7	8.6	15	1.42
Ethyl†	515.5	10	2011.5	17	58.9	11	231.0	19	11.4	11.2	21.1	12	1.91
Ferro	260.8	12	1009.0	16	11.8	26	46.6	47	4.5	4.0	16.7	10	3.40
Freeport-McMoRan	558.8	22	1944.6	28	59.9	2	310.1	25	10.7	12.8	39.3	8	4.13
Fuller (H. B.) (1)	180.9	18	685.0	15	4.8	-34	21.1	-18	2.7	4.8	12.0	12	2.20
GAF	225.0	8	961.4	15	21.8	12	90.8	-9	9.7	9.3	15.2	16	3.18
Georgia Gulf	283.6	40	1060.6	50	54.4	55	193.6	111	19.2	17.4	75.7	7	6.75
Goodrich (B. F.)	617.7	16	2416.7	19	41.5	74	209.9	151	6.7	4.5	19.9	6	7.99
Grace (W. R.)	1651.6	27	5786.1	28	55.5	4	192.1	35	3.4	4.1	13.2	12	2.26
Great American Management (5)	351.3**	80	1379.1	73	11.1	NM	23.8	NM	3.2	NM	12.5	10	2.33
Great Lakes Chemical†	141.9	6	557.8	17	27.5	57	103.3	86	19.4	13.2	22.6	11	5.93
Hanna (M. A.)†	241.2	10	1019.0	122	13.1	34	83.2	129	5.4	4.4	20.8	7	3.48
Hercules	749.0	10	2802.0	4	6.5	-83	120.4	-85	0.9	5.6	5.9	18	2.55
Himont (2)	446.5	34	1710.8	47	101.3	70	372.9	64	22.7	17.9	27.5	7	5.71
IMC Fertilizer Group (6)	310.8	23	1185.2	21	37.0	29	124.4	66	11.9	11.3	16.2	10	4.70
Intl. Minerals & Chemical (6)	241.0	-48	1044.1	-42	15.0	-68	78.7	-13	6.2	10.1	6.5	15	2.56
Lubrizol	277.6	14	1125.7	10	74.4	488	131.2	61	26.8	5.2	21.3	11	3.40
Monsanto	1881.0	2	8293.0	9	45.0	2	591.0	36	2.4	2.4	15.6	11	8.27
Morton Thiokol (6)	631.9	8	2461.1	14	38.9	-1	159.7	5	6.2	6.7	14.1	13	3.34
Nalco Chemical	262.0	14	994.1	18	28.1	27	106.0	32	10.7	9.6	22.2	13	2.70
Olin	623.0	24	2308.0	20	21.0	28	98.0	26	3.4	3.3	14.5	11	4.63
Pennwalt	263.5	23	1023.6	21	13.2	104	48.3	46	5.0	3.0	9.5	31	3.87
Quantum Chemical	806.7	21	2921.9	29	91.4	44	360.1	174	11.3	9.6	44.8	4	13.71
Rexene (9)	183.7	24	719.1	39	29.9	5	129.5	66	16.3	19.2	NA	5	4.11
Rohm & Haas	594.6	12	2535.0	15	42.3	15	230.1	18	7.1	6.9	19.1	10	3.46
Schulman (A.) (4)	160.6	12	614.9	23	6.8	16	28.6	33	4.2	4.1	18.1	14	3.20
Sterling Chemicals (3)	165.6	20	726.8	48	47.0	40	227.4	186	28.4	24.3	250.8	5	3.78
Union Carbide	2139.0	16	8324.0	20	219.0	852	720.0	210	10.2	1.2	44.4	6	5.31
Vista Chemical (3)	191.2	7	793.7	21	30.8	21	123.4	717	16.1	14.2	88.4	8	7.43
Witco	384.0	4	1585.9	11	20.4	57	71.6	13	5.3	3.5	12.8	11	3.05

5 CONGLOMERATES

INDUSTRY COMPOSITE	44736.6	5	163825.5	6	2238.8	7	7997.2	-6	5.0	3.8	14.5	14	2.63
Alco Standard (3)	985.5**	7	3880.9	5	21.6	8	101.6	22	2.2	2.2	14.9	12	2.15
Allied-Signal	3007.0	2	11909.0	7	104.0	35	463.0	-10	3.5	2.6	14.2	11	3.10
Dart Group (11)	188.1	95	540.8	43	9.7	NM	22.3	NM	5.1	NM	9.0	8	12.17
Figgie International	342.6	14	1200.2	14	21.4	19	61.9	25	6.2	6.0	16.9	10	9.03
Fuqua Industries†	223.3	35	933.6	38	-15.5	NM	76.7	78	NM	5.7	18.5	8	3.55
General Electric	12300.0	2	38820.0	-1	1011.0	NA	3386.0	14	8.2	NA	19.1	12	3.75
Greyhound	838.4**	17	3304.9	32	23.8	29	93.3	13	2.8	2.6	9.4	12	2.42
Gulf & Western (2)	935.6	-7	3055.9	5	144.0	11	384.7	8	15.4	13.0	16.9	13	3.21
Household International	352.0	23	1277.8	19	47.8	19	183.7	12	13.6	14.0	4.1	13	4.98
Itel	508.5	45	1692.6	33	0.2	-97	24.8	59	0.0	1.8	2.0	48	0.44
LTV	1670.4	-16	7324.7	-3	95.3	-32	-890.6	NM	5.7	7.1	NM	NM	-8.97
Minnesota Mining & Mfg.	2579.0	9	10581.0	12	272.0	26	1154.0	26	10.5	9.1	21.2	13	5.09
National Intergroup (9)	778.6	14	2975.2	-22	12.4	392	-39.7	NM	1.6	0.4	-6.6	NM	-2.09
Ogden	340.8	28	1087.8	21	11.4	23	57.8	21	3.3	3.5	13.3	19	1.44
Penn Central	468.6	26	1546.5	23	19.3	NM	94.1	210	4.1	NM	5.3	18	1.33
Premark International	651.2	5	2397.0	9	31.9	20	121.2	70	4.9	4.3	17.0	9	3.50
Rockwell International (3)	2869.3	7	12134.1	2	160.0	-17	779.0	15	5.6	7.2	20.7	7	2.95
Standard Shares (10)	189.2	14	766.9	17	3.4	10	17.7	-29	1.8	1.9	10.3	15	6.72
Teledyne	977.2	21	3534.6	10	98.2	-38	391.8	4	10.0	19.7	18.3	10	34.03
Tenneco	3600.0	11	13234.0	11	-177.0	NM	-1.0	NM	NM	NM	-0.7	NM	-0.18
Textron†	1985.6	5	7285.5	2	72.0	30	272.1	4	3.6	2.9	11.7	9	3.10
TRW	1712.0	-2	6982.0	2	56.0	-15	261.0	7	3.3	3.8	16.9	10	4.29
Tyler	167.7	7	664.6	6	0.8	-87	14.6	-38	0.5	3.6	26.5	9	0.77
USX	4410.0*	4	16877.0	13	158.0	NM	756.0	267	3.6	NM	14.0	12	2.62
Valhi	560.7	7	2252.4	63	35.5	166	80.6	85	6.3	2.6	26.0	18	0.70
Whitman	1035.4	14	3582.5	17	71.3	-34	176.7	-1	6.9	11.8	11.3	20	1.66
Wickes (11)	1059.8	4	3984.6	6	-49.7	NM	-46.1	NM	NM	1.9	-4.4	NM	-1.06

6 CONSUMER PRODUCTS

INDUSTRY COMPOSITE	48438.6	13	181437.7	13	2588.2	-1	11066.1	23	5.3	6.1	22.8	14	3.13
GROUP COMPOSITE	4447.3	10	17548.5	14	230.7	-12	951.8	1	5.2	6.5	30.1	10	1.67
Brown Group (11)	483.4	8	1767.6	10	11.8	-24	39.4	-13	2.4	3.5	11.1	15	2.26
Fruit of the Loom	243.3	9	1004.7	15	36.6	190	73.0	93	15.0	5.6	32.6	7	1.19
Hartmarx (1)	309.9	6	1174.3	9	15.3	-2	38.0	-8	4.9	5.3	10.9	13	2.03
Interco (10)	683.3	0	2745.6	3	0.3	NM	90.7	-35	0.0	6.1	NM	2	2.37
Kellwood (8)	190.2	-3	706.0	12	8.8	6	31.3	11	4.6	4.2	17.5	10	2.74
Leslie Fay	165.2	29	682.7	17	4.7	-23	22.3	13	2.8	4.8	17.3	10	1.17

Footnotes on page 65

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The Germans build performance and luxury at prices that offend even those who can afford to make the payments.

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Performance. Room. Character. Value. All at prices that while not inexpensive are at least realistic. (Saabs are intelligently priced from \$16,995 to \$32,095.*)

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Drive a Saab before you sign up for prestige that isn't practical, or a sensible car that's boring.

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**The most recent report of the Highway Loss Data Institute reports Saab 900 and 9000 models had lowest injury loss experience in their respective classes. Your dealer has details.



CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE- EARNINGS RATIO 2-28	12 MONTH EARNING PER SHARE
	4th QUARTER 1988 \$ MIL.	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL.	CHANGE FROM 1987 %	4th QUARTER 1988 \$ MIL.	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL.	CHANGE FROM 1987 %	4th QUARTER 1988 %	4th QUARTER 1987 %			
Liz Claiborne	290.2	22	1184.2	12	26.6	18	110.3	-4	9.2	9.4	25.4	13	1.26
Nike (7)	322.0	37	1518.9	59	24.8	34	139.8	135	7.7	7.9	28.8	8	3.73
Oxford Industries (7)	154.1	2	589.9	1	2.7	NM	-4.6	NM	1.8	NM	-4.3	NM	-0.40
Phillips-Van Heusen (11)	210.4	16	631.6	44	12.7	-11	18.3	-24	6.1	7.9	32.2	14	1.08
Reebok International	330.6	-3	1785.9	29	6.7	-80	137.0	-17	2.0	10.1	19.9	11	1.20
Russell	151.4	14	531.1	11	17.5	18	53.8	16	11.5	11.1	17.4	14	1.36
Salant (1)	157.6	292	370.6	172	9.4	281	7.6	10	6.0	6.2	34.6	12	2.10
Tulstex (1)	150.6	19	339.1	-3	14.5	10	21.2	-26	9.7	10.4	15.3	13	0.77
VLF	605.0	-2	2516.1	-2	38.2	-13	173.7	-3	6.3	7.1	16.3	12	2.55
(b) APPLIANCES & HOME FURNISHINGS													
GROUP COMPOSITE	4834.3	11	18808.6	11	178.6	1	697.4	18	3.7	4.1	15.1	14	1.61
Allegheny International (3)	227.0	-11	938.5	3	1.8	-63	-28.1	NM	0.8	1.9	NM	NM	-5.37
Armstrong World Industries	706.9	17	2680.3	13	34.6	3	162.7	8	4.9	5.5	18.1	11	3.51
Best Buy (9)	172.0	7	507.5	26	3.6	141	3.9	-21	2.1	0.9	6.6	21	0.47
Circuit City Stores (10)	434.3	23	1618.9	30	13.7	53	63.0	43	3.1	2.5	25.9	14	2.79
Emerson Radio (9)	216.8	9	721.7	-9	3.2	925	5.3	NM	1.5	0.2	6.0	28	0.15
Highland Superstores (11)	205.2	24	864.4	22	0.9	-25	6.5	-44	0.4	0.7	5.0	19	0.36
Intermark (9)†	169.8**	25	709.8	20	7.2	NM	20.0	559	4.2	NM	34.5	6	2.52
InterTan (6)	202.2	17	612.9	19	16.9	104	31.5	NM	8.4	4.8	19.5	12	3.52
Kimball International (6)	149.5	13	546.1	8	8.7	-8	31.6	-9	5.8	7.1	13.4	11	1.50
La-Z-Boy Chair (8)	144.6	19	531.1	20	8.2	11	27.4	9	5.7	6.1	15.1	12	1.52
Leggett & Platt	211.3	24	809.9	19	9.3	2	37.7	-2	4.4	5.4	15.7	12	2.21
Maytag	477.4	12	1890.0	4	33.1	13	135.5	-8	6.9	6.9	28.9	12	1.77
Ohio Mattress (1)	178.7	6	661.5	11	10.5	34	33.2	42	5.9	4.6	12.7	22	1.00
SSMC	169.2**	-6	668.4	3	-18.6	NM	-14.6	NM	NM	5.8	-8.1	NM	-2.47
Toro (5)	145.2	13	626.2	14	4.7	11	20.5	15	3.2	3.3	22.8	10	1.90
Whirlpool	1024.2	4	4421.4	5	40.9	-2	161.3	-14	4.0	4.3	12.0	11	2.33
(c) BEVERAGES													
GROUP COMPOSITE	10668.0	15	39682.0	14	649.3	24	2908.1	19	6.1	5.6	21.8	15	2.42
Anheuser-Busch	2187.8	7	8924.1	7	125.5	15	715.9	16	5.7	5.3	23.4	14	2.45
Brown-Forman (8)	303.0	-2	1046.7	-4	42.1	14	112.8	12	13.9	12.0	23.0	16	3.85
Coca-Cola	2026.8	2	8337.8	9	235.5	22	1044.7	14	11.6	9.7	33.1	17	2.85
Coca-Cola Enterprises	895.2	15	3874.4	16	58.8	310	152.6	73	6.6	1.8	7.8	15	1.03
Coors (Adolph)	353.5	21	1521.7	13	2.2	-39	46.9	-3	0.6	1.2	4.4	14	1.28
General Cinema (2)	543.5	109	2323.8	124	2.1	-93	82.9	-4	0.4	11.4	13.5	22	1.12
Johnston Coca-Cola (2)	169.9	12	646.4	21	-4.7	NM	-9.9	NM	NM	NM	-12.0	NA	NA
PepsiCo	4188.3	22	13007.0	14	187.7	30	762.2	26	4.5	4.2	25.7	14	2.90
(d) PERSONAL CARE													
GROUP COMPOSITE	10315.7	11	38967.9	14	578.5	-6	2206.3	57	5.6	6.7	19.6	14	3.52
Alberto-Culver (3)	162.5	22	633.6	18	5.5	-19	25.6	18	3.4	5.1	19.0	18	1.93
Avon Products	1011.2	17	3063.0	18	56.6	-65	121.1	-47	5.6	19.0	67.1	14	1.66
Bausch & Lomb	264.3	25	978.3	16	28.9	15	97.9	15	10.9	12.0	16.5	14	3.27
Chemed	146.2	47	500.6	28	3.7	-22	20.6	1	2.5	4.7	17.7	15	2.23
Clorox (6)	289.2	19	1354.0	14	24.4	13	138.5	15	8.4	8.9	18.3	13	2.54
Colgate-Palmolive	1212.0	6	4734.3	8	1.7	-93	152.7	NM	0.1	2.0	15.1	20	2.22
Ecolab	311.9	12	1211.9	19	14.1	64	44.1	6	4.5	3.1	10.6	17	1.63
Gillette	967.7	12	3581.2	13	61.5	5	268.5	17	6.4	6.7	NM	14	2.45
Helene Curtis Industries (10)	163.6**	36	595.6	28	3.6	82	12.8	-10	2.2	1.6	14.6	14	3.25
Intl. Flavors & Fragrances	181.3	1	839.5	13	23.2	9	128.7	20	12.8	11.9	19.3	14	3.40
Procter & Gamble (6)	5268.0	9	20368.0	14	325.0	25	1128.0	135	6.2	5.4	16.3	13	6.63
Shaklee	195.8	8	627.5	10	14.3	59	27.2	16	7.3	5.0	10.7	17	2.05
Stanhome	142.1	8	480.4	11	16.0	21	40.6	24	11.3	10.0	28.3	13	1.96
(e) TOBACCO													
GROUP COMPOSITE	18173.2	14	66431.6	13	951.2	-9	4302.5	18	5.2	6.6	26.4	13	5.99
American Brands †	3000.2*	10	11980.0	19	128.9	-2	540.8	8	4.3	4.9	22.0	12	5.44
Culbro	235.1***	1	942.5	6	-1.3	NM	0.4	-93	NM	0.5	0.3	NM	0.10
Dibrell Brothers (6)	234.1	22	607.0	48	4.7	51	13.0	NM	2.0	1.6	19.9	9	1.96
Philip Morris	8640.0*	20	31742.0	13	342.0	-28	2124.0	15	4.0	6.6	29.0	12	9.12
RJR Nabisco	4718.0	7	16956.0	8	411.0	11	1393.0	29	8.7	8.4	26.0	14	5.92
Standard Commercial (9)	289.9	28	885.8	25	0.8	-85	6.6	-54	0.3	2.2	4.7	19	0.81
Universal (6)	899.7	18	2699.8	18	25.8	5	62.5	1	2.9	3.2	17.2	9	3.69
UST	156.2*	2	618.5	7	39.4	17	162.1	24	25.2	21.9	36.8	15	1.41
7 CONTAINERS & PACKAGING													
INDUSTRY COMPOSITE	4449.1	10	17443.2	14	359.1	40	1350.5	47	8.1	6.3	23.1	8	3.96
(a) GLASS, METAL & PLASTIC													
GROUP COMPOSITE	1021.0	4	4428.9	12	1.0	-97	129.4	-27	0.1	3.7	10.7	17	1.82
Anchor Glass Container	233.7	-6	977.8	28	-9.2	NM	-8.5	NM	NM	1.5	-9.8	NM	-0.61
Ball	233.0	8	1073.0	2	-11.4	NM	32.7	-46	NM	6.0	7.7	19	1.40
Constar International	140.9	14	544.1	27	3.4	20	11.8	28	2.4	2.3	15.1	12	1.80
Crown Cork & Seal	413.4	5	1834.1	7	18.2	10	93.4	6	4.4	4.2	15.1	14	3.37

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At The Four Seasons Olympic, It's Our Grand Idea That Makes Us Seattle's Only Grand Hotel.

The Four Seasons Olympic Hotel was restored with one thought in mind. To create a grand hotel that adapts to your lifestyle. Never you to it.

Here, your needs are anticipated. So your normal routine is never compromised. That is our grand idea. And it's what we believe a grand hotel is all about.

For instance, if you like to start your day with a six a.m. dip, our solarium Spa is waiting. Swim. Sauna. Exercise. Then enjoy a leisurely breakfast. Once you've completed the business at hand, return. Relax with a massage.

Ease into the whirlpool. Recline on our private sun deck.

Also experience the personal care shown by all our staff. Take our Chef de cuisine. He understands your tastes. And your hesitation to indulge. So, he created a unique Alternative Cuisine menu... featuring this area's famous fresh food specialties. The result: gourmet cuisine, sans gourmet calories.

Most hotels would consider a full health spa and special menu unnecessary luxuries. To us, it's only a small part of a grand idea. An idea based on a simple philosophy. We adapt to you. Not the other

way around. That's why our gracious accommodations are considered such an exceptional value.

To reserve your grand experience call (800) 332-3442 or, in Seattle, (206) 621-1700.



**Four Seasons
Olympic
SEATTLE**

Power



T5200: 20MHz 386 processor, 2 internal IBM®-compatible expansion slots, VGA gas plasma display with VGA monitor port, 40MB or 100MB hard disk, 2MB RAM standard expandable to 8MB, 1.44MB 3½" diskette drive.

At Toshiba, we're not only committed to making computers more portable, but also to making portables more powerful.

Which is why, in our effort to constantly improve and refine our machines, we've added three new computers to what is already the most complete family of truly portables available.

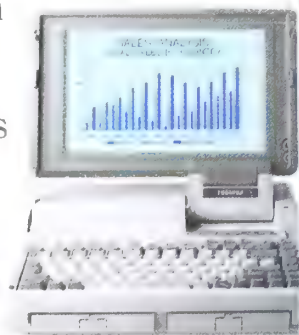
Each designed to be powerful enough to take on the increasingly complex tasks that face today's sophisticated PC users.

First, the T1600 which weighs under 12 pounds and which is the fastest battery-

powered computer we've ever made.

Second, the T3100e, the successor to our most popular machine—the T3100/20. We've made it nearly two pounds lighter and a lot faster—we've even added expansion capabilities. About the only thing we didn't add was more size.

T1600: Battery-powered 286/12MHz, coprocessor socket, 20MB hard disk at 27msec, 1.44MB 3½" diskette drive, 1MB RAM expandable to 5MB, detachable backlit EGA compatible LCD, removable rechargeable battery pack.



Surge.



And finally, the T5200, which has enough power to replace virtually any desktop PC.

But we haven't just concentrated on power and portability. We've also constantly looked for ways to make our machines more durable, more reliable, and easier to use—down to the 800 number our customers can call for help with any technical question that might come up.

We figure that's what our users demand.

And it's by anticipating the growing needs of our users that we have continually found ways to make our machines weigh

less and do more. So you can work wherever you want and however you want.

All of which might make it tempting for some people to abandon their desktop for the convenience of portability. Go ahead.

We've given you the power to do it.

T3100e: 12MHz 286 with 80287 co-processor socket, internal half-length IBM slot, 20MB hard disk with 27 msec access, 1MB RAM expandable to 5MB, gas plasma display, 1.44MB 3 1/2" diskette drive.



In Touch with Tomorrow
TOSHIBA

Toshiba America Inc., Information Systems Division

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE- EARNINGS RATIO 2-28	12 MONTHS EARNING PER SHARE
	4th QUARTER 1988 \$ MIL	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL	CHANGE FROM 1987 %	4th QUARTER 1988 \$ MIL	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL	CHANGE FROM 1987 %	4th QUARTER 1988 %	4th QUARTER 1987 %			
(b) PAPER CONTAINERS													
GROUP COMPOSITE	3428.1	12	13014.2	15	358.1	62	1221.0	65	10.4	7.2	26.4	7	4.49
Bemis	270.5	12	1069.0	15	12.6	24	39.6	24	4.7	4.2	17.1	17	1.48
Federal Paper Board	368.7	16	1116.9	9	57.9	130	143.3	94	15.7	7.9	26.1	7	3.51
Gaylord Container (3)	182.7	33	716.2	36	12.4	85	47.6	88	6.8	4.9	32.9	1	10.64
Jefferson Smurfit†	312.0	7	1255.3	14	38.3	22	144.5	57	12.3	10.8	49.7	8	3.72
Longview Fibre (2)	180.2	19	657.2	15	22.7	21	96.3	48	12.6	12.4	27.3	7	8.71
Potlatch	285.4	13	1084.1	9	33.0	33	112.4	28	11.6	9.9	18.5	8	4.01
Sonoco Products	403.9	7	1599.8	22	24.4	102	96.3	57	6.0	3.2	22.2	17	2.20
Stone Container	980.0	8	3742.2	16	109.3	88	341.8	112	11.2	6.4	35.6	6	5.69
Temple-Inland	444.7	12	1773.5	11	47.5	41	199.2	41	10.7	8.5	18.9	7	7.15
B DISCOUNT & FASHION RETAILING													
INDUSTRY COMPOSITE	58960.3	12	220060.7	11	1626.0	-10	6185.6	-2	2.8	3.4	13.8	16	1.92
Ames Department Stores (11)	524.1	7	2158.8	10	10.7	45	41.3	105	2.0	1.5	9.2	14	1.10
Best Products (11)	433.6	2	2055.9	0	-5.8	NM	21.0	-16	NM	NM	5.4	NA	0.80
Burlington Coat Factory (2)	166.9	20	574.9	20	4.5	19	21.7	7	2.7	2.7	12.6	10	1.85
Carson Pirie Scott (11)	300.1**	25	1122.0	30	2.2	-59	1.8	-79	0.7	2.2	0.2	79	0.17
Carter Hawley Hale Stores (5)	636.7**	4	2643.3	-5	-4.0	NM	4.7	NM	NM	0.1	NM	40	0.21
Charming Shoppes (11)	175.1	8	686.6	11	8.6	-22	28.7	-42	4.9	6.8	13.5	29	0.57
Child World (11)	154.2	12	787.1	15	-3.3	NM	7.9	-8	NM	NM	4.3	21	0.69
Consolidated Stores (11)	147.2	2	602.7	12	4.1	253	17.6	53	2.8	0.8	12.8	20	0.39
Costco Wholesale (4)	579.3	39	2193.6	39	3.4	516	14.5	221	0.6	0.1	13.2	34	0.56
CVN (4)	171.0	18	613.8	230	4.8	-26	9.8	24	2.8	4.4	6.3	28	0.53
Dayton Hudson (11)	2867.4**	13	11783.3	17	45.6	36	238.6	11	1.6	1.3	12.6	16	2.78
Dillard Department Stores (11)	606.2**	13	2454.9	19	17.4	19	97.9	24	2.9	2.7	14.2	15	3.04
Dollar General (11)	153.1	12	612.5	5	2.5	230	9.1	144	1.6	0.5	8.6	19	0.49
Edison Brothers Stores	325.2	7	918.6	-1	26.0	NM	36.3	NM	8.0	NM	19.0	11	3.64
Family Dollar Stores (4)	171.8	17	694.8	20	5.4	14	28.0	17	3.2	3.2	16.4	12	1.01
Gap (11)	322.8	18	1188.0	19	26.6	43	63.7	-16	8.2	6.8	25.0	23	1.76
Grossman's	285.8	11	1141.6	6	0.6	-62	13.2	-33	0.2	0.6	13.1	16	0.50
Hechinger (11)	250.6	35	945.0	36	12.1	28	46.7	24	4.8	5.1	13.2	15	1.25
Hills Department Stores (11)	443.5	8	1605.2	10	3.6	-65	10.2	-68	0.8	2.5	NM	18	0.52
Home Depot (11)	510.0	40	1848.7	37	17.1	76	73.8	61	3.4	2.7	20.2	24	1.45
Home Shopping Network (4)	200.6	8	744.6	12	6.2	99	21.1	-9	3.1	1.7	13.0	22	0.24
Jamesway (11)	190.8	12	747.8	11	4.0	8	9.8	-21	2.1	2.1	7.9	16	0.69
K mart (11)	6435.0**	7	26982.0	6	126.0	15	731.0	14	2.0	1.8	15.7	10	3.62
Limited (11)	1010.6	13	3725.4	6	70.4	2	188.3	-27	7.0	7.8	22.8	29	1.04
Lowe's (11)	652.1	1	2449.8	1	15.9	-6	58.1	-11	2.4	2.6	10.0	15	1.53
Macy (R. H.) (5)	1624.0**	20	5997.7	12	-19.0	NM	-159.6	NM	NM	0.5	NM	NA	-109.93
May Department Stores (11)	2824.0**	17	11060.0	7	104.0	21	457.0	8	3.7	3.6	16.1	12	3.05
Melville	2291.3	14	6780.4	14	205.3	27	354.5	24	9.0	8.0	23.2	12	6.51
Mercantile Stores (11)	544.2**	3	2207.7	4	40.5	7	133.6	2	7.4	7.2	14.4	12	3.63
Meyer (Fred) (11)	466.9	14	1994.8	11	5.0	12	35.1	19	1.1	1.1	14.5	12	1.45
Neiman-Marcus Group (5)	331.4	11	1256.7	8	9.9	-8	14.6	NM	3.0	3.6	NM	NM	-0.29
Nordstrom (11)	485.8	18	2164.0	18	19.9	1	109.1	27	4.1	4.8	18.3	24	1.33
Pace Membership Warehouse (11)	277.6	33	1173.8	44	1.1	213	6.4	NM	0.4	0.2	6.2	25	0.48
Penney (J. C.) (11)	3610.0	-4	14938.0	-3	160.0	-6	652.0	9	4.4	4.6	20.8	11	4.67
Petrie Stores (11)†	286.7	-5	1188.8	-6	6.1	31	40.1	-39	2.1	1.5	6.6	21	0.86
Price (4)	1603.4**	22	4432.0	24	38.9	26	102.8	26	2.4	2.4	19.7	18	2.06
Rose's Stores (11)	338.3	9	1390.6	5	4.2	-32	11.1	-55	1.2	2.0	5.7	14	0.55
Ross Stores (11)	150.0	10	600.5	8	3.6	320	20.3	NM	2.4	0.6	19.7	18	0.72
Sears, Roebuck	14563.1**	9	50251.0	9	184.1	-69	1032.3	-40	1.3	4.4	7.4	15	2.72
Service Merchandise	1296.6	13	3092.8	14	80.6	41	76.5	207	6.2	5.0	25.4	8	1.51
Spiegel	560.5**	55	1402.0	32	40.8	91	57.0	39	7.3	5.9	18.0	8	1.18
Strawbridge & Clothier (11)	205.7**	12	869.3	10	3.6	11	25.0	8	1.8	1.8	13.1	12	3.20
TJX (11)	521.8	18	1817.6	13	31.3	23	81.9	26	6.0	5.7	27.4	15	1.54
Toys 'R' Us (11)	776.8	29	3656.6	32	25.8	40	225.8	36	3.3	3.1	17.9	22	1.73
U. S. Shoe (11)	587.1	9	2273.6	5	1.3	-89	5.3	-87	0.2	2.3	1.1	NM	0.12
Wal-Mart Stores (11)	4991.1	24	19118.5	29	180.9	33	761.2	35	3.6	3.4	28.2	24	1.35
Woolworth (F. W.) (11)	1974.0**	12	7759.0	12	66.0	22	275.0	16	3.3	3.1	16.2	12	4.24
Zayre (11)	936.3	25	3355.4	-13	27.9	28	74.1	-59	3.0	2.9	13.8	18	1.33
9 ELECTRICAL & ELECTRONICS													
INDUSTRY COMPOSITE	27245.7	10	101887.8	12	880.3	-34	5225.1	9	3.2	5.4	12.6	14	2.38
(a) ELECTRICAL PRODUCTS													
GROUP COMPOSITE	7791.0	11	28368.6	11	484.0	0	1910.3	11	6.2	6.9	17.8	12	3.40
Cooper Industries	1193.2**	18	4258.2	19	74.7	32	224.4	29	6.3	5.6	13.2	12	4.41
Emerson Electric (3)	1719.8	9	6793.1	8	136.8	10	540.7	12	8.0	7.9	18.7	13	2.38
Hubbell	154.9	6	614.2	6	18.4	8	71.3	14	11.9	11.6	18.7	14	2.49
National Service Industries (4)	371.8	9	1444.1	7	22.9	10	88.2	12	6.2	6.1	15.4	13	1.80
Raychem (6)	276.8	0	1102.7	8	15.2	-43	102.8	15	5.5	9.7	14.2	11	2.98
Square D	426.4	12	1656.8	12	26.0	34	118.9	8	6.1	5.1	18.8	12	4.44
Westinghouse Electric	3648.2	11	12499.5	10	189.9	-14	764.0	5	5.2	6.7	19.8	11	5.20

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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12/31	PRICE EARNINGS RATIO 2/28	12 MONTHS' EARNINGS PER SHARE
	4th QUARTER 1988 \$ MIL	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL	CHANGE FROM 1987 %	4th QUARTER 1988 \$ MIL	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL	CHANGE FROM 1987 %	4th QUARTER 1988 %	4th QUARTER 1987 %			
ELECTRONICS													
GROUP COMPOSITE	10541.6	11	39543.2	11	558.2	14	2222.0	20	5.3	5.1	13.3	12	2.88
3M Systems	388.0	23	1439.0	17	20.4	15	74.6	23	5.3	5.6	15.8	12	2.40
General Instrument (10)	359.3	21	1268.3	15	21.9	10	84.3	57	6.1	6.7	13.8	13	2.52
3M Hughes Electronics	3005.8	13	11001.0	6	169.5	16	783.4	17	5.6	5.5	10.4	14	1.96
Harris (6)	555.2	13	2104.8	11	25.2	10	69.6	-22	4.5	4.6	7.1	16	1.79
Litton Industries (5)	1228.8	3	4896.0	8	43.6	7	170.0	18	3.5	3.4	14.4	11	6.51
Motorola (9)	378.5	1	1493.4	20	22.0	18	85.2	23	5.8	5.0	17.9	10	3.41
Motorola	2193.0**	19	8250.0	23	124.0	22	445.0	44	5.7	5.5	13.6	12	3.43
Raytheon	2209.0	3	8191.9	7	127.3	8	489.6	10	5.8	5.5	24.3	9	7.35
TRC Systems (6)	223.9	29	898.9	46	4.4	11	20.3	19	2.0	2.3	12.5	14	0.97
INSTRUMENTS													
GROUP COMPOSITE	4414.0	8	16602.3	10	-386.3	NM	-159.7	NM	NM	2.4	-2.8	NM	-0.68
Foxboro	143.1	14	539.9	7	3.9	NM	9.8	NM	2.7	NM	5.3	38	0.80
General Signal	463.6	10	1760.2	10	20.7	-2	25.2	-64	4.5	5.0	2.7	54	0.91
Honeywell	1929.9	-3	7148.3	7	-482.8	NM	-434.9	NM	NM	4.3	-19.5	NM	-10.22
Johnson Controls (3)	860.4	17	3227.2	18	30.8	4	104.6	19	3.6	4.1	11.8	12	2.86
Mark IV Industries (10)	237.0	115	569.7	55	4.8	20	22.7	47	2.0	3.6	20.2	5	2.10
Millipore	170.5	11	621.9	18	16.8	7	54.5	14	9.8	10.2	15.6	16	1.96
Perkin-Elmer (5)	273.5	6	1304.1	6	12.3	7	66.9	230	4.5	4.5	8.8	15	1.52
Tektronix (7)	336.2	6	1431.0	3	7.3	51	-8.6	NM	2.2	1.5	-1.7	NM	-0.23
SEMICONDUCTORS													
GROUP COMPOSITE	4499.1	12	17374.0	21	224.5	-14	1252.5	56	5.0	6.5	15.8	13	1.98
Advanced Micro Devices	248.1	-6	1125.9	13	-34.1	NM	19.3	NM	NM	NM	1.4	75	0.11
AMP	695.0	10	2669.3	15	85.0	21	319.0	28	12.2	11.1	21.3	15	2.96
Intel	727.3**	27	2874.8	51	85.8	-10	452.9	83	11.8	16.7	21.8	10	2.51
Molex (6)	144.0	17	549.6	26	8.4	-41	56.3	12	5.8	11.6	14.5	16	2.22
National Semiconductor (7)	705.3	10	2666.8	29	-25.2	NM	-16.1	NM	NM	1.8	-3.2	NM	-0.27
Texas Instruments	1692.1	10	6294.8	13	95.3	5	366.3	14	5.6	5.9	19.5	10	4.05
Varian Associates (3)	287.4	8	1192.9	15	9.3	NM	54.7	NM	3.3	NM	12.1	11	2.51
FOOD													
INDUSTRY COMPOSITE	64919.4	16	242511.8	11	1419.5	2	5485.4	6	2.2	2.5	19.4	15	1.87
FOOD DISTRIBUTION													
GROUP COMPOSITE	10637.3	28	38915.0	16	110.5	43	381.5	20	1.0	0.9	14.0	16	1.66
Di Giorgio	287.4	15	1045.5	10	2.6	-21	9.5	-10	0.9	1.3	12.2	16	1.68
Farm House Foods (9)	152.0	-11	694.0	-6	-1.3	NM	-24.3	NM	NM	NM	NM	NM	-2.69
Investment Foods	161.9	9	634.6	14	-1.4	NM	3.4	12	NM	0.3	5.5	25	0.36
Fleming	3110.7	49	10467.0	21	21.1	635	65.4	32	0.7	0.1	12.0	13	2.43
Nash Finch	507.5**	10	2097.8	8	3.3	-48	18.2	-2	0.7	1.4	12.2	13	1.67
Rykoff-Sexton (8)	332.6	15	1222.3	11	5.8	29	19.2	61	1.7	1.6	11.2	16	1.62
Super Food Services (4)	390.9**	9	1604.0	5	3.5	13	14.9	19	0.9	0.9	15.6	13	2.07
Super Rite Foods (10)	194.5	18	714.1	13	1.6	18	7.0	66	0.8	0.8	16.9	17	1.40
Super Valu Stores (10)	2464.6	10	10024.7	7	34.4	27	129.5	19	1.4	1.2	17.3	14	1.73
Sysco (6)	1733.5	62	5561.0	39	27.5	28	96.8	44	1.6	2.0	16.3	19	2.16
Wetterau (9)	1301.6	25	4849.8	23	13.3	12	42.0	12	1.0	1.1	18.9	14	1.75
FOOD PROCESSING													
GROUP COMPOSITE	28764.0	13	107719.0	10	1232.1	16	4177.4	12	4.3	4.2	19.0	15	2.42
Beatrice (10)	1152.0	4	4089.0	6	-2.0	NM	-29.0	NM	NM	NM	-3.5	NA	-0.12
Borden	1983.3	10	7243.5	11	93.9	15	311.9	17	4.7	4.5	17.7	13	4.22
Campbell Soup (5)	1333.1	13	5022.9	10	69.4	11	248.6	-1	5.2	5.3	12.8	17	1.92
Castle & Cooke	588.8	38	2469.2	33	19.4	0	112.3	26	3.3	4.5	14.5	13	2.05
ConAgra (7)	2809.5	22	10341.4	12	56.8	17	171.7	16	2.0	2.1	19.2	14	2.15
CPC International	1176.3	11	4700.0	-4	82.4	7	289.1	-19	7.0	7.3	25.4	14	3.68
Curtice-Burns Foods (6)	212.1	10	723.6	6	4.8	30	15.8	39	2.2	1.9	17.5	10	2.84
Dean Foods (7)	433.7	10	1612.3	8	13.7	12	54.2	20	3.2	3.1	16.6	15	2.03
Flowers Industries (6)	179.0	7	752.8	-3	8.1	-6	41.0	25	4.5	5.1	20.0	14	1.17
General Mills (7)	1415.8	9	5314.7	2	79.6	7	290.4	13	5.6	5.7	33.6	16	3.48
Gerber Products (9)	240.4	6	1016.6	11	19.1	56	76.7	54	7.9	5.4	21.0	16	3.88
Heinz (H. J.) (8)	1424.6	12	5525.8	12	109.9	14	412.8	14	7.7	7.5	25.9	15	3.13
Hershey Foods	672.2	26	2168.0	16	46.2	29	144.5	16	6.9	6.7	14.9	16	1.60
Holly Farms (7)	479.4	25	1798.4	17	22.2	161	69.0	59	4.6	2.2	15.6	16	3.83
Hormel (Geo. A.) (2)	655.4	-12	2292.8	-1	28.8	43	60.2	31	4.4	2.7	14.4	13	1.57
JPB	2378.9	21	9066.1	18	22.8	47	62.3	-8	1.0	0.8	13.1	12	1.32
Imperial Holly (9)	176.0	206	609.0	NA	10.9	NM	13.3	NA	6.2	0.8	14.5	7	3.40
International Multifoods (10)	508.5	10	1846.9	14	11.3	6	35.9	25	2.2	2.3	11.5	11	2.46
Kellogg	1092.1	13	4348.9	15	100.9	23	480.4	21	9.2	8.5	34.3	15	3.90
McCormick (1)	349.3	8	1183.9	10	17.3	29	35.6	46	5.0	4.1	12.0	17	1.53
Pilgrim's Pride (3)	149.9	52	557.8	35	0.9	NM	-1.7	NM	0.6	NM	-2.5	NM	-0.07
Pillsbury (7)	1745.0	4	6277.0	1	44.8	-38	42.2	-80	2.6	4.3	3.0	NA	0.50
Quaker Oats (6)	1349.6	10	5615.6	15	41.4	-9	259.2	24	3.1	3.7	20.1	16	3.26
Ralston Purina (3)	1681.1	11	6000.4	2	131.4	8	362.4	4	7.8	8.1	33.3	15	5.30

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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE- EARNINGS RATIO 2-28	12 MONTH EARNINGS PER SHARE
	4th QUARTER 1988 \$ MIL	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL	CHANGE FROM 1987 %	4th QUARTER 1988 \$ MIL	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL	CHANGE FROM 1987 %	4th QUARTER 1988 %	4th QUARTER 1987 %			
Sara Lee (6)	3075.4	16	11206.3	16	137.3	39	376.9	28	4.5	3.7	20.0	14	3.25
Savannah Foods & Industries	258.9	11	916.9	4	10.6	153	20.1	43	4.1	1.8	15.9	15	3.00
Smithfield Foods (6)	201.8	-21	812.6	-20	2.9	-34	17.0	96	1.4	1.7	40.3	7	1.97
Thorn Apple Valley (7)	149.0	1	592.9	-1	3.1	2	4.0	NM	2.1	2.1	15.4	6	1.15
Tyson Foods (3)	502.4	15	2000.6	11	19.9	12	83.5	19	4.0	4.1	23.2	12	1.30
Universal Foods (3)	187.7	0	721.9	1	10.8	26	29.9	14	5.8	4.6	16.2	18	1.83
Wrigley (Wm.) Jr.	202.6	10	891.4	14	13.6	5	87.2	24	6.7	7.0	28.3	17	2.18
(c) FOOD RETAILING													
GROUP COMPOSITE	25518.0	15	95878.5	11	76.9	-70	926.5	-18	0.3	1.2	26.2	18	0.92
Albertson's (11)	1669.2	14	6404.3	11	38.1	41	151.0	30	2.3	1.8	20.0	18	2.27
American Stores (11)	4941.7	42	16901.3	19	20.7	-44	124.1	-24	0.4	1.1	11.1	17	3.33
Big Bear (4)	250.1	11	954.9	9	3.2	-23	15.3	6	1.3	1.9	13.8	22	1.70
Borman's (11)	239.2	9	1035.8	-1	-9.7	NM	-26.0	NM	NM	NM	NM	NA	-9.24
Bruno's (6)	569.8	18	2361.7	30	12.9	14	45.6	16	2.3	2.3	16.4	20	0.55
Circle K (8)	837.8**	24	2943.2	17	13.3	-7	48.5	-4	1.6	2.1	14.8	15	0.97
Dairy Mart Convenience (11)	174.1*	-2	707.6	0	1.3	-11	4.5	NM	0.7	0.8	14.2	9	1.02
Delchamps (6)	225.0	7	886.6	7	-0.1	NM	9.4	38	NM	0.5	12.6	16	1.36
Food Lion	1262.3	30	3815.4	29	34.3	22	112.5	31	2.7	2.9	28.0	29	0.35
Giant Food (10)	685.8	11	2903.6	8	21.4	21	89.4	41	3.1	2.9	22.4	15	1.48
Great Atlantic & Pacific Tea (10)	2302.4	5	9867.5	2	29.5	26	122.3	24	1.3	1.1	13.0	15	3.20
Hannaford Brothers	353.8**	31	1261.7	22	6.8	27	28.9	20	1.9	2.0	18.0	8	3.08
Ingles Markets (3)	210.9	15	808.1	17	3.1	-11	13.8	44	1.5	1.9	12.1	11	0.77
Kruger	4647.9	5	19053.0	8	-119.0	NM	34.5	-81	NM	1.1	NM	40	0.24
Marsh Supermarkets (9)	213.6	9	893.6	9	2.5	31	8.2	3	1.2	1.0	13.6	16	1.05
Mayfair Super Markets (4)	146.0	10	586.5	17	2.1	-3	11.9	22	1.4	1.6	26.3	12	1.53
National Convenience Stores (6)	271.9	36	1036.7	21	-2.1	NM	-3.1	NM	NM	0.6	-4.0	NM	-0.13
Penn Traffic (11)	414.5**	162	917.5	48	-7.7	NM	-3.9	NM	NM	0.5	-11.9	NM	-0.90
Ruddick (3)	312.0	18	1158.6	16	3.9	-1	18.4	18	1.3	1.5	12.7	12	1.89
Stop & Shop (11)	1052.5	7	4572.7	8	-19.1	NM	-32.6	NM	NM	0.9	-42.7	NA	-1.68
Supermarkets General (11)	1481.1	4	5896.0	3	-17.7	NM	-63.6	NM	NM	NM	NM	NA	-75.56
Village Super Market (5)	146.0	10	635.1	10	1.3	8	6.2	34	0.9	0.9	12.8	11	1.87
Weis Markets	327.5	13	1189.2	5	23.3	11	82.6	9	7.1	7.2	16.7	16	1.82
Winn-Dixie Stores (6)	2782.0	2	9088.3	3	34.6	25	128.3	12	1.2	1.0	17.2	14	3.19
11 FUEL													
INDUSTRY COMPOSITE	89977.8	-1	356418.0	5	4292.6	NM	16939.8	114	4.8	NM	12.6	12	3.39
(a) COAL													
GROUP COMPOSITE	1341.1	30	4782.3	24	104.2	NM	327.3	NM	7.8	NM	15.0	8	2.79
Cyprus Minerals	413.1	80	1327.1	67	65.4	553	170.0	550	15.8	4.3	17.3	6	6.31
Nacco Industries	183.9	67	616.5	32	8.9	42	45.0	32	4.9	5.7	19.2	7	5.08
Nerco	178.7	18	661.8	5	13.1	-10	75.6	26	7.3	9.6	19.2	7	2.26
Pittston	413.0**	4	1583.4	15	11.8	NM	36.8	NM	2.8	NM	8.4	19	0.95
Westmoreland Coal	152.4	9	593.5	2	5.0	NM	-0.1	NM	3.3	NM	-0.1	NM	-0.02
(b) OIL & GAS													
GROUP COMPOSITE	83733.9	-2	332652.8	4	3948.7	NM	15728.4	106	4.7	NM	12.8	12	3.73
Amerasia Hess	1193.8**	-6	4263.5	-11	66.3	NM	124.2	-46	5.6	NM	5.8	23	1.51
American Petrofina	675.5**	1	2634.7	6	32.9	142	132.9	60	4.9	2.0	16.5	7	10.07
Amoco	5526.0	4	21157.0	5	375.0	-1	2063.0	52	6.8	7.1	15.7	10	8.01
Ashland Oil (3)	2018.9	7	7951.9	8	95.9	140	239.6	64	4.7	2.1	20.0	8	4.30
Atlantic Richfield	4548.0**	-2	18324.0	8	391.0	15	1583.0	29	8.6	7.4	25.9	10	8.78
Burlington Resources	476.2	-21	2167.3	-9	50.6	-19	69.6	-70	10.6	10.3	2.4	NM	0.46
Chevron	6900.0**	-7	28900.0	-1	175.0	-25	1768.0	41	2.5	3.2	11.9	9	5.17
Coastal	2112.4	3	8236.5	11	71.1	103	157.4	39	3.4	1.7	12.3	12	2.70
Crown Central Petroleum	280.5	-3	1149.3	6	15.5	NM	38.4	NM	5.5	NM	15.3	6	4.70
Diamond Shamrock R&M	449.5	-4	1803.9	4	27.4	NM	54.3	472	6.1	0.4	15.3	8	2.14
Exxon	20135.0**	-3	80213.9	3	1380.0	-11	5260.0	9	6.9	7.5	16.8	11	3.95
Kerr-McGee	689.5	8	2743.2	5	33.4	127	110.1	31	4.9	2.3	7.9	18	2.27
Louisiana Land & Exploration	152.1**	-32	726.3	-12	1.0	-86	-70.2	NM	0.7	3.1	-14.1	NM	-2.27
Mapco	457.1**	-4	1802.4	10	29.9	146	117.1	105	6.5	2.6	20.0	11	5.88
Mitchell Energy & Dev. (11)	140.5	2	580.6	3	-2.4	NM	0.4	-94	NM	1.0	0.1	NM	0.01
Mobil	13886.0***	-2	54877.0	7	448.0	14	2038.0	67	3.2	2.8	13.3	9	4.95
Murphy Oil	415.5**	7	1525.1	0	25.7	NM	38.7	NM	6.2	NM	5.4	31	1.14
Occidental Petroleum	5284.0	20	19417.0	14	7.0	-70	313.0	70	0.1	0.5	4.8	22	1.26
Pacific Resources	207.8**	-8	881.8	-8	10.0	NM	27.9	586	4.8	NM	12.9	13	1.40
Pennzoil	624.8**	25	2273.9	24	36.1	88	-187.0	NM	5.8	3.8	-15.1	NM	-5.22
Phillips Petroleum	2810.0	-2	11304.0	5	135.0	309	650.0	NM	4.8	1.2	31.9	8	2.72
Quaker State	204.6	-3	869.1	-4	5.8	70	14.9	NM	2.8	1.6	4.7	32	0.57
Sun	2720.0**	4	10000.0	2	76.0	-8	7.0	-98	2.8	3.2	0.1	NM	0.06
Sun Exploration & Production	316.0**	-20	1286.0	-9	2.0	-95	-305.0	NM	0.6	9.4	-23.8	NM	-2.58
Tesoro Petroleum (3)	146.6**	-57	978.8	-28	3.1	NM	-9.6	NM	2.1	NM	-11.5	NM	-1.33
Texaco	8469.0**	-10	31338.0	-1	296.0	NM	1304.0	NM	3.5	NM	13.3	10	5.35
Tosco	242.1	-25	1142.5	-4	5.8	-47	55.2	99	2.4	3.4	75.6	6	0.65
Union Texas Petroleum	254.8	-18	1152.0	-10	14.8	18	109.3	96	5.8	4.0	41.0	17	0.73
Unocal	2398.0**	11	9154.0	5	141.0	386	24.0	-87	5.9	1.3	1.2	NM	0.21

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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12/31	PRICE- EARNINGS RATIO 2/28	12 MONTHS' EARNINGS PER SHARE	
	4th QUARTER 1988 \$ MIL.	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL.	CHANGE FROM 1987 %	4th QUARTER 1988 \$ MIL.	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL.	CHANGE FROM 1987 %	4th QUARTER 1988 %	4th QUARTER 1987 %				
PETROLEUM SERVICES														
GROUP COMPOSITE	4902.9	11	18983.1	20	239.7	-43	884.1	171	4.9	9.6	8.5	24	1.21	
Baker Hughes (3)	566.3	4	2336.2	16	15.6	-8	58.1	NM	2.7	3.1	5.3	35	0.44	
Cameron Iron Works (6)	153.9	16	559.4	19	5.3	NM	2.9	NM	3.5	NM	-0.8	NM	-0.08	
CBI Industries	358.3**	13	1375.7	19	2.4	-67	27.5	50	0.7	2.3	4.5	32	0.87	
Dresser Industries (2)	973.2	12	3941.7	26	60.9	164	122.8	653	6.3	2.7	8.2	19	1.78	
Halliburton	1375.3**	24	4838.7	26	11.8	-65	84.6	76	0.9	3.1	4.0	35	0.81	
NL Industries	235.4	12	1007.0	17	47.1	54	134.2	53	20.0	14.5	NM	10	2.25	
Schlumberger	1240.5	1	4924.5	12	96.7	-69	453.9	-10	7.8	25.7	12.1	21	1.72	
HEALTH CARE														
INDUSTRY COMPOSITE	31475.6	10	123542.7	11	2531.2	751	10254.6	42	8.0	1.0	24.0	16	2.72	
DRUG DISTRIBUTION														
GROUP COMPOSITE	7718.8	12	30089.6	12	85.6	18	353.4	6	1.1	1.1	10.3	16	1.00	
Alco Health Services (3)	552.5**	10	2105.8	15	3.8	-31	18.4	-3	0.7	1.1	9.5	18	1.38	
Anac Holding (7)	572.0	6	2503.7	2	-17.9	NM	-106.0	NM	NM	NM	NM	NA	-28.66	
Bergen Brunswig (4)	967.9**	17	3626.7	14	12.0	66	37.6	103	1.2	0.9	16.4	12	2.04	
Bindley Western Industries	360.8	21	1275.0	21	0.6	NM	3.6	85	0.2	NM	7.8	12	0.58	
Cardinal Distribution (9)	182.8	36	652.1	20	2.2	58	7.3	50	1.2	1.0	11.2	14	1.31	
Durr-Fillauer Medical	156.9	19	587.7	18	3.6	42	11.4	52	2.3	1.9	18.7	12	1.52	
Hook-SupeRx (4)	413.4	49	1415.0	NA	-6.3	NM	-10.6	NA	NM	NM	-66.6	NA	-0.31	
Longs Drug Stores (1)	461.3	8	1872.6	7	11.6	10	54.0	19	2.5	2.5	18.1	13	2.64	
McKesson (9)	1797.7**	5	7051.9	8	24.0	9	91.1	21	1.3	1.3	13.1	14	2.14	
Medco Containment Services (6)	179.3	53	606.1	45	6.9	27	24.6	54	3.9	4.7	9.4	25	0.53	
Perry Drug Stores (2)	168.0	11	667.0	13	3.8	NM	-8.4	NM	2.2	NM	-19.5	NM	-0.83	
Rite Aid (10)	694.5	7	2745.6	21	16.5	-18	95.3	10	2.4	3.1	15.6	15	2.31	
Walgreen (4)	1211.7	9	4980.4	12	24.7	31	135.0	24	2.0	1.7	18.6	16	2.19	
DRUGS & RESEARCH														
GROUP COMPOSITE	10532.9	10	41044.7	12	1546.4	44	5988.1	17	14.7	11.2	27.6	17	3.43	
American Home Products	1300.9	7	5500.5	9	238.6	11	932.2	10	18.3	17.7	33.0	13	6.38	
Lilly (Eli)	1042.3	15	4069.7	12	175.7	NM	761.0	85	16.9	NM	23.5	18	5.33	
Marion Laboratories (6)	220.0	22	826.6	19	53.8	49	181.0	45	24.5	20.0	43.1	19	1.17	
Merck	1534.1	10	5939.5	17	307.3	32	1206.8	33	20.0	16.7	45.2	21	3.05	
Pfizer	1368.2	7	5385.4	9	141.6	4	791.3	15	10.3	10.7	18.6	12	4.70	
Rorer Group	325.2	16	1041.6	12	26.9	20	61.8	14	8.3	8.0	14.8	20	1.96	
Schering-Plough	739.9	12	2969.4	10	92.9	24	389.8	23	12.6	11.3	24.3	17	3.48	
SmithKline Beckman	1276.9	7	4749.0	10	159.4	12	229.2	-60	12.5	11.8	14.8	27	1.84	
Squibb	664.8	12	2585.8	20	97.5	15	425.5	19	14.7	14.3	32.1	16	4.30	
Syntex (5)	349.9	14	1315.3	12	94.5	25	315.7	21	27.0	24.6	43.4	14	2.68	
Upjohn	712.8	9	2753.5	9	80.7	14	353.4	16	11.3	10.9	20.0	16	1.90	
Warner-Lambert	997.9	11	3908.4	14	77.5	17	340.3	15	7.8	7.4	36.2	16	5.00	
HEALTH CARE SERVICES														
GROUP COMPOSITE	4796.9	10	19109.9	6	142.6	-8	688.4	47	3.0	3.6	14.7	15	1.34	
American Medical Intl. (4)	646.8	-13	3016.8	9	0.4	-98	76.5	-27	0.1	3.0	10.4	18	0.96	
Beverly Enterprises	510.4	2	2025.0	-3	-11.6	NM	-23.9	NM	NM	NM	-5.2	NM	-0.47	
Charter Medical (3)	280.7	24	1046.3	22	-13.6	NM	-45.6	NM	NM	5.3	NM	NA	-2.84	
FHP International (6)	160.9	38	593.8	43	4.9	33	19.3	163	3.1	3.2	42.4	10	1.89	
Hospital Corp. of America	1022.7	11	4111.2	-12	53.3	62	258.8	NM	5.2	3.6	16.4	13	3.62	
Humana (4)	938.5	18	3580.3	17	54.6	9	231.6	20	5.8	6.3	19.8	12	2.34	
Manor Care (7)	149.5	12	564.9	10	5.1	-42	-7.9	NM	3.4	6.7	-4.1	NM	-0.21	
National Medical Enterprises (7)	894.6**	16	3432.8	15	47.3	8	174.4	11	5.3	5.7	16.8	11	2.38	
U. S. Healthcare	192.7**	18	738.9	18	2.1	-62	5.3	405	1.1	3.3	3.8	65	0.12	
MEDICAL PRODUCTS														
GROUP COMPOSITE	8427.0	9	33299.3	13	756.6	NM	3224.7	155	9.0	NM	24.6	16	2.73	
Abbott Laboratories	1306.3	6	4937.0	13	222.3	17	752.0	19	17.0	15.4	32.8	15	3.33	
Bard (C. R.)	191.9	15	757.5	18	20.7	26	78.7	26	10.8	9.8	24.6	16	1.38	
Baxter International	1825.0	11	6861.0	10	121.0	34	388.0	20	6.6	5.5	12.1	14	1.31	
Becton Dickinson (3)	406.1	11	1823.5	14	23.0	11	157.2	19	5.7	5.7	15.3	14	3.75	
Bristol-Myers	1479.5	9	5972.5	11	195.5	12	829.0	17	13.2	12.8	23.8	16	2.88	
Cooper (2)	160.2	-9	611.3	72	-57.5	NM	-152.0	NM	NM	2.0	NM	NM	-7.01	
Fisher Scientific Group	245.9	4	957.7	5	9.8	-12	38.3	24	4.0	4.7	12.1	16	1.04	
Johnson & Johnson	2200.0	8	9000.0	12	184.0	13	974.0	17	8.4	8.0	27.8	15	5.72	
Medtronic (8)	181.2	19	713.5	27	22.7	5	92.7	16	12.5	14.2	21.5	12	6.95	
Owens & Minor	189.9	21	731.6	27	2.1	2	8.4	29	1.1	1.3	11.1	14	1.00	
Robins (A. H.)	241.0	3	933.8	9	12.9	NM	58.4	NM	5.4	NM	NM	11	2.42	
HOUSING & REAL ESTATE														
INDUSTRY COMPOSITE	11380.5	8	44424.1	13	298.7	-36	1890.1	-18	2.6	4.4	16.2	12	2.04	
BUILDING MATERIALS														
GROUP COMPOSITE	8328.9	9	32599.1	9	428.3	0	2094.7	0	5.1	5.6	23.1	10	2.93	
CalMat	161.4**	5	660.8	-1	12.3	-20	56.4	-28	7.6	10.1	11.9	16	1.82	
Georgia-Pacific	2567.0	15	9509.0	11	129.0	15	467.0	2	5.0	5.0	18.2	8	4.76	
Lafarge	332.5	5	1309.2	7	20.4	32	93.5	30	6.1	4.9	13.9	8	1.96	

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE- EARNINGS RATIO 2-28	12 MONTHS' EARNINGS PER SHARE
	4th QUARTER 1988 \$ MIL.	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL.	CHANGE FROM 1987 %	4th QUARTER 1988 \$ MIL.	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL.	CHANGE FROM 1987 %	4th QUARTER 1988 %	4th QUARTER 1987 %			
Manville	522.1	7	2062.2	7	-27.9	NM	89.1	-43	NM	6.0	5.4	10	0.73
Masco	609.6	12	2438.6	21	49.3	60	288.3	32	8.1	5.7	18.6	12	2.10
Owens-Corning Fiberglas	704.0	-1	2831.0	-2	58.0	49	197.0	-10	8.2	5.5	NM	6	4.71
PPG Industries	1432.0	8	5616.7	8	102.3	6	467.6	24	7.1	7.3	21.9	10	4.26
Scotty's (6)	140.9	6	562.6	7	2.5	-6	4.3	-62	1.8	2.0	2.5	44	0.29
Sherwin-Williams	444.6	8	1950.5	8	18.7	-4	101.1	8	4.2	4.8	16.6	11	2.30
Southdown	169.8**	106	595.5	74	13.6	61	37.1	-18	8.0	10.3	12.0	8	2.33
Tecumseh Products	259.2	11	1093.5	15	18.0	0	70.2	-2	6.9	7.7	11.6	11	12.84
Texas Industries (7)	178.3	12	668.4	11	5.3	224	14.4	738	3.0	1.0	4.7	27	1.21
USG	540.0	-6	2248.0	0	1.6	-82	72.7	-58	0.3	1.6	NM	4	1.38
Vulcan Materials	267.4	9	1053.2	14	25.1	-12	136.0	19	9.4	11.6	21.8	13	13.19
(b) CONSTRUCTION & REAL ESTATE													
GROUP COMPOSITE	3051.6	4	11825.0	26	-129.6	NM	-204.6	NM	NM	1.4	-11.1	NM	-1.32
Blount (10)	277.6**	-9	1187.4	6	-63.2	NM	-72.1	NM	NM	NM	-50.9	NM	-6.00
Centex (9)	456.3**	29	1729.7	26	9.8	61	31.9	22	2.2	1.7	8.5	13	2.10
Kaufman & Broad (11)	548.8	8	2050.3	35	-8.5	NM	24.2	-60	NM	4.1	6.3	19	0.76
Kaufman & Broad Home (1)	254.3	-3	903.4	34	17.1	9	48.0	35	6.7	6.0	22.6	9	1.76
Perini	184.8	-10	848.9	14	-5.8	NM	4.4	-61	NM	2.9	1.8	48	0.71
Ryland Group	342.6**	4	1271.9	0	10.5	117	40.7	26	3.1	1.5	25.5	7	3.10
Southmark (6)	794.2**	5	3097.6	69	-92.8	NM	-288.2	NM	NM	1.4	-48.9	NM	-7.20
U. S. Home	193.1	-9	735.8	-13	3.1	NM	6.5	NM	1.6	NM	3.6	13	0.16
14 LEISURE TIME INDUSTRIES													
INDUSTRY COMPOSITE	18836.2	17	68906.0	18	1000.7	28	4424.7	20	5.3	4.8	19.0	15	2.49
(a) EATING PLACES													
GROUP COMPOSITE	3227.2	11	12377.7	20	192.4	12	833.4	18	6.0	5.9	19.8	15	2.05
Jerrico (6)	161.4**	2	648.7	5	5.8	11	18.4	-24	3.6	3.3	8.0	18	0.95
McDonald's	1451.2	15	5566.3	14	151.5	17	645.9	18	10.4	10.2	19.7	15	3.43
Morrison (7)	206.8**	16	744.3	25	8.1	16	28.9	26	3.9	3.9	16.5	15	1.61
Shoney's (2)	203.7**	21	782.1	13	3.1	-73	44.9	-9	1.5	6.9	NM	7	1.22
TW Services	945.5	9	3573.7	44	17.2	15	66.8	18	1.8	1.7	13.5	21	1.36
Wendy's International	258.6	0	1062.6	0	6.8	102	28.5	721	2.6	1.3	6.8	22	0.30
(b) ENTERTAINMENT													
GROUP COMPOSITE	3371.7	29	11640.1	24	285.6	32	1067.7	34	8.5	8.3	18.3	20	2.54
Disney (Walt) (3)	1043.6	42	3747.2	27	148.3	48	569.9	35	14.2	13.7	24.2	18	4.14
MCA	962.1**	43	3023.7	17	75.7	247	164.9	20	7.9	3.2	10.1	22	2.26
MGM/UA Communications (4)	170.3	-6	663.3	39	-39.5	NM	-90.3	NM	NM	1.1	-49.7	NM	-1.78
Warner Communications	1195.7	17	4206.1	24	101.1	10	423.2	29	8.5	9.0	25.2	16	2.65
(c) HOTEL & MOTEL													
GROUP COMPOSITE	3219.0	9	10760.3	9	108.4	-21	550.7	3	3.4	4.7	52.9	14	2.54
Caesars World (5)	230.8	3	840.1	3	22.7	-23	70.1	27	9.8	13.2	35.9	10	2.87
Hilton Hotels	254.4**	15	953.6	13	35.2	-40	130.9	-6	13.8	26.4	16.6	18	2.72
Holiday	367.8**	-4	1596.6	-4	-14.5	NM	117.2	-1	NM	NM	NM	6	4.70
Marriott	2366.1	12	7370.0	13	65.0	5	232.5	4	2.7	2.9	32.1	16	1.95
(d) OTHER LEISURE													
GROUP COMPOSITE	9018.3	18	34127.9	19	414.3	63	1972.9	21	4.6	3.3	16.1	13	2.68
American Greetings (10)	382.1	4	1246.2	8	12.1	-34	30.7	-36	3.2	5.0	5.5	22	0.95
Bally Mfg.	476.7**	10	1940.8	12	-7.1	NM	38.0	NM	NM	NM	5.1	21	1.12
Brunswick	752.0	-6	3282.0	6	17.0	-50	193.1	14	2.3	4.2	20.5	8	2.20
Coleman	141.0	6	657.9	10	1.8	-7	24.5	28	1.2	1.4	12.0	20	3.47
Eastman Kodak†	4543.0	29	17034.0	28	312.0	29	1397.0	19	6.9	6.9	21.1	11	4.31
Fleetwood Enterprises (8)	419.5	16	1529.6	12	21.1	91	63.1	36	5.0	3.0	16.7	9	2.75
Gibson Greetings	167.0	15	404.3	12	14.4	27	35.0	45	8.6	7.8	20.4	10	2.25
Harley-Davidson	197.6	18	757.4	11	6.0	37	27.2	54	3.1	2.6	23.3	7	3.41
Harman International (6)	142.6	19	504.1	27	4.6	29	13.7	28	3.2	3.0	18.1	11	1.59
Hasbro	394.9	4	1357.9	1	21.1	211	72.4	50	5.3	1.8	10.3	14	1.24
Mattel	287.6	23	990.0	-3	10.5	NM	35.9	NM	3.6	NM	27.5	14	0.75
Outboard Marine (3)	307.7	19	1653.2	20	1.0	-53	70.7	27	0.3	0.8	12.2	9	3.68
Polaroid	533.2	5	1862.9	6	-7.5	NM	-22.6	NM	NM	8.3	-2.2	NM	-0.34
Tonka	273.4	31	907.7	137	7.4	NM	-5.8	NM	2.7	NM	-6.6	NM	-0.75
15 MANUFACTURING													
INDUSTRY COMPOSITE	19571.4	12	73494.0	16	856.2	27	3213.1	80	4.4	3.9	13.5	14	2.29
(a) GENERAL MANUFACTURING													
GROUP COMPOSITE	5797.2	11	21742.8	14	228.5	-31	973.0	65	3.9	6.4	13.0	17	1.61
Avery International (1)	416.6	8	1582.0	8	21.1	NM	77.7	124	5.1	NM	15.3	12	1.77
Corning Glass Works†	543.0	1	2121.5	2	51.4	-9	292.4	55	9.5	10.5	18.7	10	3.25
Crane	343.9	24	1313.1	19	12.5	64	49.2	50	3.6	2.8	17.7	11	2.17
Emhart	723.0	9	2762.3	13	33.0	25	126.1	18	4.6	4.0	14.6	20	2.02
Harsco	358.1	-8	1300.0	8	-18.0	NM	31.1	-51	NM	4.8	7.0	21	1.17
Hillenbrand Industries (1)	248.3	24	884.3	22	17.4	0	69.7	21	7.0	8.8	19.7	14	1.86
Illinois Tool Works	489.6	8	1929.8	14	34.3	28	140.0	32	7.0	5.9	18.8	13	2.66
Jostens (a)	176.2	34	609.4	15	9.6	21	46.3	28	5.5	6.1	26.2	15	1.29

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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON EQUITY		
	Q4	CHANGE	Q4	CHANGE	Q4	CHANGE	Q4	CHANGE	Q4	Q4	Q4	Q4	Q4
	QUARTER	FROM	QUARTER	FROM	QUARTER	FROM	QUARTER	FROM	QUARTER	QUARTER	QUARTER	QUARTER	QUARTER
	\$ MIL.	%	\$ MIL.	%	\$ MIL.	%	\$ MIL.	%	%	%	%	%	%
Marley	182.6	24	581.4	NA	16.7	209	-38.9	NA	9.1	3.4	NM	NA	-6.40
McDermott International	614.0	1	2307.7	-2	-31.8	NM	-119.6	NM	NM	19.2	-18.0	NM	-3.22
Newell	253.7	-2	988.0	37	20.0	58	61.4	65	8.4	5.2	21.4	14	2.78
Norton	351.6	2	1410.0	10	16.7	71	55.2	38	4.5	4.1	15.0	12	4.06
Philips Industries	203.8	41	808.7	28	9.1	11	45.7	6	4.0	5.1	19.2	12	1.60
Robertson (H. H.)	140.4	36	418.7	32	1.0	NM	-39.0	NM	0.8	NM	-48.7	NM	-5.08
Rubbermaid	287.9	10	1190.0	18	21.1	14	99.3	17	7.3	7.2	20.0	20	1.66
Trinity Industries	236.3**	38	816.1	40	8.9	95	25.4	249	3.5	2.3	18.0	15	1.40
Valmont Industries	186.0	36	601.1	49	5.0	121	15.3	85	0.7	1.7	20.6	10	0.76
MACHINE & HAND TOOLS GROUP COMPOSITE	1976.5	11	7273.9	13	118.2	NM	390.2	163	6.0	NM	15.4	14	2.11
Black & Decker	705.5	15	2374.2	18	38.4	23	104.3	60	5.4	5.1	13.7	13	1.77
Cincinnati Milacron	207.9	-2	887.6	4	7.8	NM	15.0	NM	3.4	NM	1.8	22	1.00
Clark Equipment	345.6	4	1278.3	21	14.4	NM	34.1	NM	4.0	NM	11.3	13	2.59
Snap-on Tools	291.3**	8	864.6	13	27.2	14	113.0	28	12.9	12.2	22.5	13	2.72
Stanley Works	486.2	6	1909.0	8	30.4	16	103.5	7	5.2	5.7	15.5	12	2.40
SPECIAL MACHINERY GROUP COMPOSITE	8371.5	15	31566.8	23	459.7	42	1622.8	99	5.5	4.4	14.6	12	3.47
Briggs & Stratton	207.8	-15	902.9	4	-1.9	NM	14.0	-53	NM	3.0	5.0	28	0.48
Caterpillar	2662.0	17	10435.0	26	163.0	17	616.0	93	6.1	6.1	15.0	10	6.67
Deere	148.4	12	5364.8	30	80.5	147	286.7	NM	5.4	2.5	11.7	12	4.00
Dover	581.3	15	1953.8	23	37.3	19	146.8	31	7.4	7.0	20.6	13	2.13
FMC	880.1	3	3286.9	5	36.0	553	129.2	-32	4.1	0.6	NM	11	3.60
Harnischfeger Industries	316.4	13	1208.6	24	9.8	206	32.5	150	3.1	1.1	7.1	15	1.15
Imo Delaval	198.7	90	587.2	87	9.0	95	28.3	51	4.5	4.4	10.0	11	1.78
Ingersoll-Rand	815.1	10	3021.4	14	58.3	34	161.6	50	7.2	5.9	13.0	12	3.00
Interlake	245.2	10	892.2	8	10.5	-46	39.6	27	5.2	10.6	14.8	11	3.76
Stewart & Stevenson Services	145.4	105	467.6	56	7.3	143	21.1	150	5.0	4.2	21.9	10	3.07
Timken	409.1	20	1554.1	26	24.8	209	66.9	588	5.1	3.4	6.8	15	2.34
Tyco Laboratories	505.9	22	1770.5	43	22.9	47	82.0	80	4.5	3.7	16.4	15	3.23
TEXTILES GROUP COMPOSITE	3426.2	6	12910.7	5	49.8	70	227.1	1	1.5	0.9	8.5	15	1.53
Amoskeag	377.6**	-4	1176.5	-4	1.8	NM	3.6	NM	0.5	NM	2.5	20	1.08
Burlington Holdings	171.4	-23	3174.6	-20	-16.5	NM	-30.3	NM	NM	NM	-31.5	NA	-2.43
Dixie Yarns	20.9	-7	506.4	4	5.1	-27	21.5	-18	3.4	4.3	10.0	10	1.80
DWG	282.6	10	1127.7	3	-0.6	NM	3.7	84	NM	0.3	1.0	58	0.93
Fieldcrest Cannon	107.8	-4	1188.2	-4	5.1	NM	11.3	NM	1.4	NM	4.3	20	1.10
Guilford Mills	144.0	6	592.4	6	3.4	-27	25.6	0	2.4	3.3	13.2	11	2.60
Interface	150.2	100	396.7	49	6.0	-47	20.2	47	4.0	5.7	16.1	14	1.18
Shaw Industries	274.3	38	1100.0	48	11.1	58	40.3	46	4.0	3.5	23.7	9	2.61
Springs Industries	484.0	16	1514.6	10	20.5	43	50.8	-45	4.9	3.6	9.8	10	2.98
West Point-Pepperell	680.1	42	2160.3	34	10.8	-47	79.4	15	1.6	4.3	10.3	20	2.69
16 METALS & MINING													
INDUSTRY COMPOSITE	12141.0	21	46383.8	24	1165.2	394	4125.4	136	9.6	2.4	25.8	6	5.13
ALUMINUM GROUP COMPOSITE	5105.5	24	19306.4	25	646.8	2995	2084.3	315	12.7	0.5	27.2	5	9.06
Aluminum Co. of America	1646.5	29	6777.0	25	216.7	66	561.4	265	6.3	6.5	19.8	6	9.72
Alcoa	1466.7	10	5744.0	17	288.2	NM	740.9	360	28.9	NM	53.5	3	6.42
Reynolds Metals	492.3	27	6807.1	20	109.9	114	482.0	140	9.6	5.7	25.1	6	9.01
STEEL GROUP COMPOSITE	5162.1	15	20226.3	19	260.2	111	1218.7	116	5.0	2.7	22.2	6	3.67
Allegheny Ludlum	144.2	36	507.7	39	20.5	26	108.6	108	8.0	4.6	37.9	7	4.81
Amco	401.1	16	2121.1	10	40.3	-20	190.1	17	4.9	6.6	15.1	8	1.40
Bethlehem Steel	100.2	11	1449.8	19	65.7	NM	391.6	107	4.9	0.1	25.0	5	5.46
Carpenter Technology	25.1	30	637.8	23	8.0	105	33.0	140	5.5	3.2	10.0	14	3.62
Commercial Metals	326.7	74	1111.4	36	8.3	26	17.1	24	2.5	1.7	15.6	9	2.54
Cyclops Industries	286.4	23	1024.9	15	8.9	NM	96.5	48	3.1	NM	113.6	5	4.15
Inland Steel Industries	1037.1	13	4169.1	18	17.5	63	148.8	100	5.5	3.8	4.9	5	6.44
Lone Star Technologies	222.9	41	644.1	57	-17.7	NM	-24.8	NM	NM	4.0	-8.6	NM	-1.24
Lukens	31.6	17	605.0	30	9.6	46	33.4	64	6.0	4.9	19.4	7	2.91
Wheeling-Pittsburgh Steel	274.8	10	1110.1	10	42.3	NM	176.8	240	14.7	NM	NM	3	30.76
Worthington Industries	144.0	75	95.0	18	14.6	16	51.4	20	6.0	5.9	20.0	15	1.80
OTHER METALS GROUP COMPOSITE	1873.4	33	6851.1	36	258.2	182	822.4	20	13.8	6.5	28.4	8	3.31
Asarco	599.3	38	1884.7	47	70.1	31	287.1	48	10.0	18.0	16.7	5	4.42
Inspiration Resources	246.4**	48	216.3	40	8.8	NM	40.1	670	7.1	NM	10.3	13	0.63
Magma Copper	184.0	30	607.1	30	3.5	NM	56.3	NM	6.0	NM	13.0	5	1.50
Newmont Mining	10.1	51	444.0	38	26.4	NM	96.7	145	17.3	NM	NM	30	1.40
Phelps Dodge	686.2	38	2319.8	44	140.6	60	420.2	178	20.5	17.0	27.2	4	10.16

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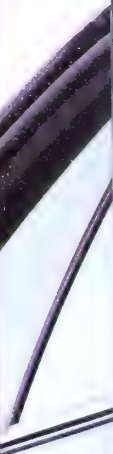
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It's called the Audi Advantage.* And it's no mere warranty. Instead, it's as close as anyone has come to risk-free, worry-free ownership.

And it's standard equipment on every new Audi. No charge. No deductibles. No excuses.

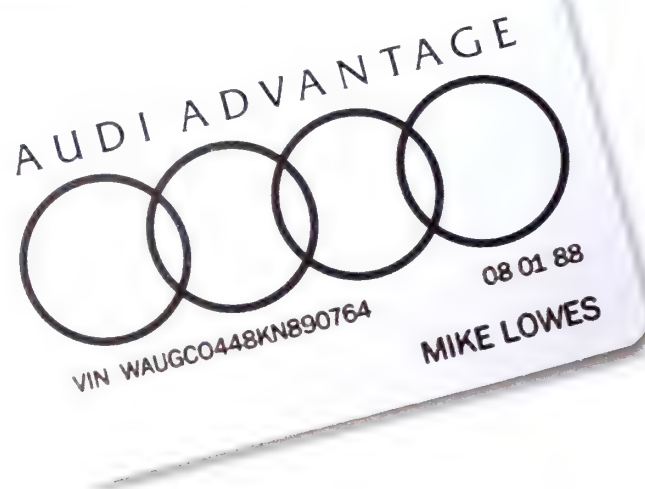
How does it work? For starters, the no-charge maintenance and limited warranty of the Audi Advantage means all repairs, all scheduled maintenance, all routine oil changes are *all paid for* — for 3 years or 50,000 miles. Even normal wear items, like brake pads and wiper blades, are covered.

In short, it pays for virtually everything but gasoline. (An owner still has a few responsibilities, of course; so there's some inevitable fine print about negligence and accidents.)

The Audi Advantage also provides 10 years of corrosion protection. 24-Hour Roadside Assistance. And welcome security at trade-in time. Thanks to a Guaranteed Resale Index that certifies trade-in value.

It is a most impressive list. One no other car maker can match. And one more reason to take the alternate route.

Even The Protection Plan Pursues A Different Path.



*Your dealer will proudly share details of Audi's new car and corrosion perforation limited warranties, and the other programs listed above. Roadside Assistance is provided by the United States Auto Club Motoring Division, Inc. Guaranteed Resale Index excludes leases. Certain restrictions apply. Not all features described are available on every model. For more information, call 1-800-FOR-AUDI. © 1989 Audi.

CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12/31	PRICE EARNINGS RATIO 2/28	'12 MONTHS' EARNINGS PER SHARE
	4th QUARTER 1988 \$ MIL	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL	CHANGE FROM 1987 %	4th QUARTER 1988 \$ MIL	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL	CHANGE FROM 1987 %	4th QUARTER 1988 %	4th QUARTER 1987 %			
NONBANK FINANCIAL													
INDUSTRY COMPOSITE	65456.3	13	252522.6	12	3476.5	56	12621.3	9	5.3	3.8	13.7	10	3.64
FINANCIAL SERVICES GROUP COMPOSITE	26076.9	24	95864.5	18	1269.0	231	4769.7	40	4.9	1.8	17.5	11	3.51
Alexander & Alexander	317.9	6	1227.7	4	20.4	91	71.0	-5	6.4	3.6	19.7	14	1.71
Alleghany	274.7	4	1006.0	-7	13.4	4	46.0	-30	4.9	4.9	8.6	11	7.27
American Express	6345.0**	33	22934.0	30	221.0	NM	988.0	135	3.5	NM	20.9	13	2.31
Equifax	199.8	13	743.1	11	8.4	-4	34.0	11	4.2	5.0	15.7	18	1.47
Federal Natl. Mortgage Assn.	2741.4**	1	10635.2	6	152.7	-22	506.7	35	5.6	7.2	23.8	9	6.43
Loews	2960.2**	14	10865.3	17	264.1	-1	890.4	36	8.9	10.3	23.4	7	11.70
Lomas Financial (d)	338.0**	9	1283.1	33	0.9	NM	-72.7	NM	0.3	NM	-33.5	NM	-2.00
Marsh & McLennan	544.4**	6	2272.4	6	50.6	-4	296.3	-2	9.3	10.2	39.8	14	4.09
Merrill Lynch	2849.7**	21	10547.2	7	275.8	NM	463.2	25	9.7	0.1	13.3	7	4.29
Morgan Stanley Group	1161.3**	62	4108.8	31	108.3	245	394.6	71	9.3	4.4	31.7	6	10.26
PaineWebber Group	696.2	29	2512.3	3	0.5	-93	42.4	-43	0.1	1.3	2.4	32	0.58
Primerica	291.5**	24	1003.7	10	67.5	129	161.8	59	23.2	12.6	22.0	6	3.61
Salomon	1813.0**	36	6146.0	2	-38.0	NM	280.0	97	NM	NM	7.5	16	1.65
Shearson Lehman Hutton	2915.0**	63	10529.0	56	-13.5	NM	96.5	-4	NM	NM	5.4	26	0.81
Student Loan Marketing Assn.	636.6	42	2172.0	37	58.9	23	225.1	24	9.3	10.6	36.8	17	5.34
Transamerica	1992.3**	3	7879.0	8	78.0	3	346.4	-1	3.9	3.9	12.8	8	4.42
INSURANCE													
GROUP COMPOSITE	32679.4	5	131623.5	8	1919.4	22	6605.9	-1	5.9	5.0	12.6	9	4.15
Aetna Life & Casualty	5595.9	-7	24296.4	5	197.1	-14	667.7	-23	3.5	3.8	10.3	8	5.85
American Family	604.0	16	2324.6	24	29.7	17	108.9	17	4.9	4.9	17.5	11	1.35
American General	1087.0	35	3846.0	13	107.0	37	413.0	6	9.8	9.7	9.4	10	3.22
American International Group	3648.7	10	13613.2	19	325.0	20	1175.1	24	8.9	8.2	17.6	10	7.14
American National Insurance	191.3	17	933.7	9	18.5	230	94.2	4	9.7	3.4	5.6	11	3.33
Aon	728.6	-2	2732.4	11	52.9	18	204.4	10	7.3	6.1	16.7	9	3.18
Capital Holding	567.8	40	2045.9	15	63.4	313	189.9	6	11.2	3.8	16.5	8	4.00
Chubb	1015.3	6	3980.5	7	93.4	6	372.6	8	9.2	9.2	17.1	7	8.85
Cigna	4685.1	2	17889.4	5	122.2	-30	410.2	-35	2.6	3.8	7.5	11	4.89
Conseco	111.7	-1	583.4	110	7.9	5	30.3	53	7.1	6.7	48.3	3	4.21
Fireman's Fund	908.7	3	3691.0	-16	71.0	103	247.0	-18	7.8	4.0	16.6	7	4.73
First Capital Holdings	204.1	40	735.5	65	16.4	235	52.7	67	8.0	3.3	18.5	5	1.90
General Re	634.1	-17	2735.8	-12	137.0	6	518.5	13	21.6	17.0	19.5	11	5.44
Home Group	829.1**	23	2977.8	19	17.3	-24	81.4	-32	2.1	3.4	8.3	6	2.38
Kemper	748.6**	1	3135.3	4	60.6	53	205.6	6	8.1	5.3	12.2	9	3.50
NWNL	504.4	1	2200.0	7	6.8	-23	43.9	7	1.4	1.8	10.8	8	4.01
Provident Life & Accident	788.5**	13	2827.2	12	44.7	200	85.3	451	5.7	2.1	8.1	12	1.83
Reliance Group Holdings	973.8	20	3730.4	11	-15.1	NM	23.6	-81	NM	2.0	6.2	16	0.32
Safeco	786.9**	20	3017.7	11	68.7	60	234.8	12	8.7	6.5	15.1	8	3.59
St. Paul	983.8	16	3630.8	8	87.6	8	349.3	8	8.9	9.6	18.0	7	7.26
Torchmark	423.8	7	1669.8	5	47.7	1	185.2	-8	11.3	11.9	21.4	10	3.20
Travelers	4045.0	-2	18986.3	5	237.4	141	429.6	0	5.9	2.4	9.2	9	4.14
UNUM	549.7	6	2198.5	5	37.9	112	129.3	52	6.9	3.5	9.5	10	2.86
USF&G	1471.9	9	5581.8	16	79.5	-9	305.7	-18	5.4	6.4	16.0	9	3.57
USLife	328.3	13	1279.1	8	19.6	-4	67.7	-9	6.0	7.0	7.3	10	3.81
Washington National	263.5	10	981.8	14	-15.0	NM	-20.1	NM	NM	NM	-5.4	NM	-1.90
SAVINGS & LOAN													
GROUP COMPOSITE	6700.0	19	25035.3	15	288.1	7	1245.8	-14	4.3	4.8	9.7	7	2.40
Ahmannson (H. F.)	958.7	45	3516.8	34	67.8	47	202.0	-5	7.1	7.0	11.0	8	2.04
CalFed	726.2**	9	2815.6	13	17.6	-42	134.8	-19	2.4	4.6	9.7	4	5.39
Coast Savings & Loan Assn.	295.3**	7	1110.3	6	13.2	-16	47.8	-16	4.5	5.7	9.8	5	3.63
CrossLand Savings	353.1**	20	1364.8	31	20.8	2	104.8	9	5.9	6.9	6.7	4	4.42
Dime Savings Bank of N. Y.	277.8	8	1051.1	17	6.5	-60	45.6	-31	2.3	6.4	6.4	6	2.00
Empire of America	298.7**	14	1090.3	11	-17.4	NM	-57.3	NM	NM	NM	-41.2	NM	-4.24
Glenfed (d)	642.6**	11	2474.3	10	35.2	8	154.9	16	5.5	5.6	14.5	4	5.28
Golden West Financial	393.6	25	1410.3	11	36.5	21	138.3	-10	9.3	9.6	16.1	8	4.41
Great American First Savings	459.3	25	1601.5	13	20.1	76	50.3	-43	4.4	3.1	7.9	6	2.08
Great Western Financial	841.7**	17	3164.6	11	59.7	337	248.4	17	7.1	1.9	12.7	8	1.95
HomeFed	431.4**	25	1578.5	21	32.2	71	111.3	11	7.5	5.5	12.1	6	5.22
Homestead Financial	130.2	5	490.3	-6	-0.8	NM	-9.1	NM	NM	2.1	-6.6	NM	-0.78
Imperial Corp. of America	311.7**	14	1162.3	8	-16.9	NM	10.7	-79	NM	4.7	3.9	11	0.74
Northeast Savings (d)	188.2**	18	719.0	22	-5.3	NM	-12.8	NM	NM	1.0	-7.5	NM	-4.04
Standard Federal Bank	226.5**	9	866.8	7	13.6	6	58.3	3	6.0	6.2	14.4	5	1.91
TransCapital Financial	165.1	26	618.9	19	5.3	106	17.7	45	3.2	2.0	8.7	4	1.86
OFFICE EQUIPMENT & COMPUTERS													
INDUSTRY COMPOSITE	51311.8	12	170975.6	13	4314.5	2	12497.1	7	8.4	9.2	14.8	14	3.86
BUSINESS MACHINES, SERVICES & SUPPLIES													
GROUP COMPOSITE	3464.9	13	12735.4	15	264.4	15	854.1	14	7.6	7.5	18.1	14	2.10
Automatic Data Processing (d)	409.5**	9	1616.8	10	44.0	10	178.2	19	10.7	10.7	18.8	16	2.33
Businessland (d)	301.3	17	1031.6	34	9.5	78	27.1	101	3.1	2.1	18.8	13	0.98
Deluxe	332.6	35	1196.0	26	45.0	5	143.4	-3	13.5	17.4	26.5	16	1.68

Footnotes on page 65

It's called the Audi Advantage.* And it's no mere warranty. Instead, it's as close as anyone has come to risk-free, worry-free ownership.

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In short, it pays for virtually everything but gasoline. (An owner still has a few responsibilities, of course; so there's some inevitable fine print about negligence and accidents.)

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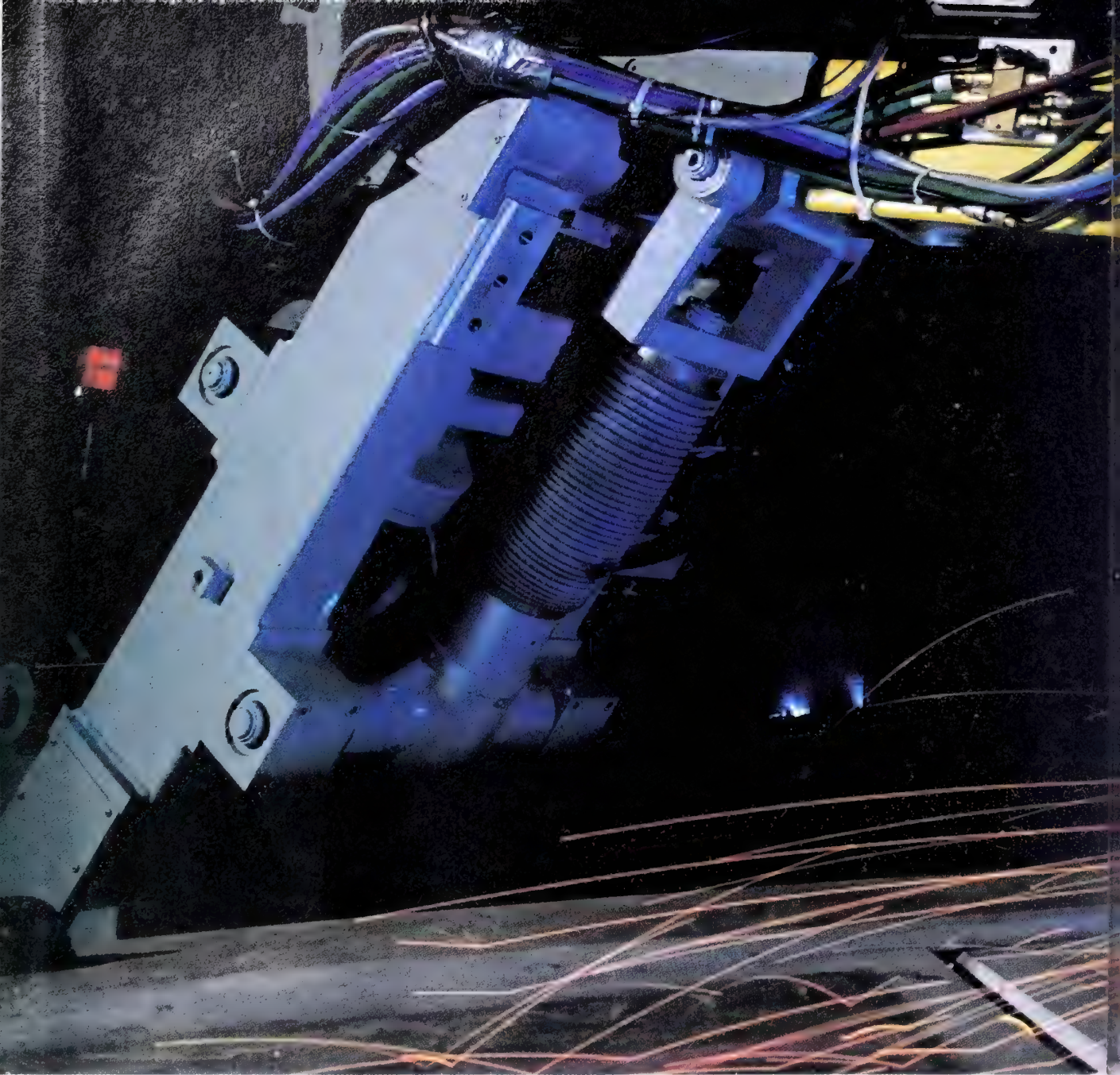


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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12/31	PRICE- EARNINGS RATIO 2/28	12 MONTHS' EARNINGS PER SHARE	
	4th QUARTER 1988 \$ MIL.	CHANGE FROM 1987	12 MONTHS 1988 \$ MIL.	CHANGE FROM 1987	4th QUARTER 1988 \$ MIL.	CHANGE FROM 1987	12 MONTHS 1988 \$ MIL.	CHANGE FROM 1987	4th QUARTER 1988	4th QUARTER 1987				
NONBANK FINANCIAL														
INDUSTRY COMPOSITE	65456.3	13	252522.6	12	3476.5	56	12621.3	9	5.3	3.8	13.7	10	3.64	
FINANCIAL SERVICES GROUP COMPOSITE	26076.9	24	95864.5	18	1269.0	231	4769.7	40	4.9	1.8	17.5	11	3.51	
Alexander & Alexander	317.9	6	1227.7	4	20.4	91	71.0	-5	6.4	3.6	19.7	14	1.71	
Alleghany	274.7	4	1006.0	-7	13.4	4	46.0	-30	4.9	4.9	8.6	11	7.27	
American Express	6345.0**	33	22934.0	30	221.0	NM	988.0	135	3.5	NM	20.9	13	2.31	
Equifax	199.8	13	743.1	11	8.4	-4	34.0	11	4.2	5.0	15.7	18	1.47	
Federal Natl. Mortgage Assn.	2741.4**	1	10635.2	6	152.7	-22	506.7	35	5.6	7.2	23.8	9	6.43	
Loews	2960.2**	14	10865.3	17	264.1	-1	890.4	36	8.9	10.3	23.4	7	11.70	
Lomas Financial (6)	338.0**	9	1283.1	33	0.9	NM	-72.7	NM	0.3	NM	-33.5	NM	-2.00	
Marsh & McLennan	544.4**	6	2272.4	6	50.6	-4	296.3	-2	9.3	10.2	39.8	14	4.09	
Merrill Lynch	2849.7**	21	10547.2	7	275.8	NM	463.2	25	9.7	0.1	13.3	7	4.29	
Morgan Stanley Group	1161.3**	62	4108.8	31	108.3	245	394.6	71	9.3	4.4	31.7	6	10.26	
PaineWebber Group	696.2	29	2512.3	3	0.5	-93	42.4	-43	0.1	1.3	2.4	32	0.58	
Primerica	291.5**	24	1003.7	10	67.5	129	161.8	59	23.2	12.6	22.0	6	3.61	
Salomon	1813.0**	36	6146.0	2	-38.0	NM	280.0	97	NM	NM	7.5	16	1.65	
Shearson Lehman Hutton	2915.0**	63	10529.0	56	-13.5	NM	96.5	-4	NM	NM	5.4	26	0.81	
Student Loan Marketing Assn.	636.6	42	2172.0	37	58.9	23	225.1	24	9.3	10.6	36.8	17	5.34	
Transamerica	1992.3**	3	7879.0	8	78.0	3	346.4	-1	3.9	3.9	12.8	8	4.42	
INSURANCE														
GROUP COMPOSITE	32679.4	5	131623.5	8	1919.4	22	6605.9	-1	5.9	5.0	12.6	9	4.15	
Aetna Life & Casualty	5595.9	-7	24296.4	5	197.1	-14	667.7	-23	3.5	3.8	10.3	8	5.85	
American Family	604.0	16	2324.6	24	29.7	17	108.9	17	4.9	4.9	17.5	11	1.35	
American General	1087.0	35	3846.0	13	107.0	37	413.0	6	9.8	9.7	9.4	10	3.22	
American International Group	3648.7	10	13613.2	19	325.0	20	1175.1	24	8.9	8.2	17.6	10	7.14	
American National Insurance	191.3	17	933.7	9	18.5	230	94.2	4	9.7	3.4	5.6	11	3.33	
Aon	728.6	-2	2732.4	11	52.9	18	204.4	10	7.3	6.1	16.7	9	3.18	
Capital Holding	567.8	40	2045.9	15	63.4	313	189.9	6	11.2	3.8	16.5	8	4.00	
Chubb	1015.3	6	3980.5	7	93.4	6	372.6	8	9.2	9.2	17.1	7	8.85	
Cigna	4685.1	2	17889.4	5	122.2	-30	410.2	-35	2.6	3.8	7.5	11	4.89	
Conseco	111.7	-1	583.4	110	7.9	5	30.3	53	7.1	6.7	48.3	3	4.21	
Fireman's Fund	908.7	3	3691.0	-16	71.0	103	247.0	-18	7.8	4.0	16.6	7	4.73	
First Capital Holdings	204.1	40	735.5	65	16.4	235	52.7	67	8.0	3.3	18.5	5	1.90	
General Re	634.1	-17	2735.8	-12	137.0	6	518.5	13	21.6	17.0	19.5	11	5.44	
Home Group	829.1**	23	2977.8	19	17.3	-24	81.4	-32	2.1	3.4	8.3	6	2.38	
Kemper	748.6**	1	3135.3	4	60.6	53	205.6	6	8.1	5.3	12.2	9	3.50	
NWNL	504.4	1	2200.0	7	6.8	-23	43.9	7	1.4	1.8	10.8	8	4.01	
Provident Life & Accident	788.5**	13	2827.2	12	44.7	200	85.3	451	5.7	2.1	8.1	12	1.83	
Reliance Group Holdings	973.8	20	3730.4	11	-15.1	NM	23.6	-81	NM	2.0	6.2	16	0.32	
Safeco	786.9**	20	3017.7	11	68.7	60	234.8	12	8.7	6.5	15.1	8	3.59	
St. Paul	983.8	16	3630.8	8	87.6	8	349.3	8	8.9	9.6	18.0	7	7.26	
Torchmark	423.8	7	1669.8	5	47.7	1	185.2	-8	11.3	11.9	21.4	10	3.20	
Travelers	4045.0	-2	18986.3	5	237.4	141	429.6	0	5.9	2.4	9.2	9	4.14	
UNUM	549.7	6	2198.5	5	37.9	112	129.3	52	6.9	3.5	9.5	10	2.86	
USF&G	1471.9	9	5581.8	16	79.5	-9	305.7	-18	5.4	6.4	16.0	9	3.57	
USLife	328.3	13	1279.1	8	19.6	-4	67.7	-9	6.0	7.0	7.3	10	3.81	
Washington National	263.5	10	981.8	14	-15.0	NM	-20.1	NM	NM	NM	-5.4	NM	-1.90	
SAVINGS & LOAN														
GROUP COMPOSITE	6700.0	19	25035.3	15	288.1	7	1245.8	-14	4.3	4.8	9.7	7	2.40	
Ahmanson (H. F.)	958.7	45	3516.8	34	67.8	47	202.0	-5	7.1	7.0	11.0	8	2.04	
CalFed	726.2**	9	2815.6	13	17.6	-42	134.8	-19	2.4	4.6	9.7	4	5.39	
Coast Savings & Loan Assn.	295.3**	7	1110.3	6	13.2	-16	47.8	-16	4.5	5.7	9.8	5	3.63	
CrossLand Savings	353.1**	20	1364.8	31	20.8	2	104.8	9	5.9	6.9	6.7	4	4.42	
Dime Savings Bank of N. Y.	277.8	8	1051.1	17	6.5	-60	45.6	-31	2.3	6.4	6.4	6	2.00	
Empire of America	298.7**	14	1090.3	11	-17.4	NM	-57.3	NM	NM	NM	-41.2	NM	-4.24	
Glenfed (6)	642.6**	11	2474.3	10	35.2	8	154.9	16	5.5	5.6	14.5	4	5.28	
Golden West Financial	393.6	25	1410.3	11	36.5	21	138.3	-10	9.3	9.6	16.1	8	4.41	
Great American First Savings	459.3	25	1601.5	13	20.1	76	50.3	-43	4.4	3.1	7.9	6	2.08	
Great Western Financial	841.7**	17	3164.6	11	59.7	337	248.4	17	7.1	1.9	12.7	8	1.95	
HomeFed	431.4**	25	1578.5	21	32.2	71	111.3	11	7.5	5.5	12.1	6	5.22	
Homestead Financial	130.2	5	490.3	-6	-0.8	NM	-9.1	NM	NM	2.1	-6.6	NM	-0.78	
Imperial Corp. of America	311.7**	14	1162.3	8	-16.9	NM	10.7	-79	NM	4.7	3.9	11	0.74	
Northeast Savings (9)	188.2**	18	719.0	22	-5.3	NM	-12.8	NM	NM	1.0	-7.5	NM	-4.04	
Standard Federal Bank	226.5**	9	866.8	7	13.6	6	58.3	3	6.0	6.2	14.4	5	1.91	
TransCapital Financial	165.1	26	618.9	19	5.3	106	17.7	45	3.2	2.0	8.7	4	1.86	
OFFICE EQUIPMENT & COMPUTERS														
INDUSTRY COMPOSITE	51311.8	12	170975.6	13	4314.5	2	12497.1	7	8.4	9.2	14.8	14	3.86	
BUSINESS MACHINES, SERVICES & SUPPLIES GROUP COMPOSITE	3464.9	13	12738.4	15	264.4	15	854.1	14	7.6	7.5	18.1	14	2.10	
Automatic Data Processing (6)	409.5**	9	1616.8	10	44.0	10	178.2	19	10.7	10.7	18.8	16	2.33	
Businessland (6)	301.3	17	1031.6	34	9.5	78	27.1	101	3.1	2.1	18.8	13	0.98	
Deluxe	332.6	35	1196.0	26	45.0	5	143.4	-3	13.5	17.4	26.5	16	1.68	

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Ah, the miracles of the modern world. Consider Robotic Vision Systems Inc.

Using specialized laser technology, they've developed a way to scan 3-D objects with incredible precision. So robots can actually see where they're going.

And how do they turn



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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE- EARNINGS RATIO 2-28	12 MONTH EARNING PER SHARE
	4th QUARTER 1988 \$ MIL.	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL.	CHANGE FROM 1987 %	4th QUARTER 1988 \$ MIL.	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL.	CHANGE FROM 1987 %	4th QUARTER 1988 %	4th QUARTER 1987 %			
Dennison Mfg.	198.0	7	721.8	2	14.0	25	38.1	9	7.1	6.1	16.0	11	2.41
Esselte Business Systems	378.7	4	1401.7	13	18.5	0	58.9	4	4.9	5.1	13.4	11	2.87
HON Industries	140.0	4	532.5	3	10.4	64	25.8	10	7.5	4.7	19.8	13	1.38
Micro D	173.3	60	553.4	57	2.7	75	8.3	50	1.6	1.4	19.5	13	1.12
Miller (Herman) (7)	205.2	12	764.9	18	11.9	2	44.2	16	5.8	6.4	17.1	12	1.81
Nashua	249.8	6	989.4	14	8.5	18	32.5	22	3.4	3.0	14.3	10	3.33
Pitney-Bowes	746.1	12	2649.9	14	78.9	17	237.0	21	10.6	10.1	18.8	14	3.00
Reynolds & Reynolds (3)	143.6	4	605.3	6	7.1	154	22.4	15	4.9	2.0	10.8	13	2.09
Standard Register	186.7	6	675.2	1	14.0	-3	38.1	-6	7.5	8.1	13.2	14	1.28
(b) COMPUTERS & PERIPHERALS													
GROUP COMPOSITE	43964.0	11	143997.3	12	3747.9	1	10672.4	6	8.5	9.4	14.2	13	4.66
Amdahl	545.7	13	1801.8	20	63.5	30	213.8	51	11.6	10.1	21.2	9	1.99
Apollo Computer	184.1	13	653.5	18	1.3	-87	0.2	-99	0.7	6.1	0.1	NM	0.01
Apple Computer (3)	1405.1	35	4434.1	46	140.5	16	419.3	50	10.0	11.6	41.8	11	3.26
Commodore International (6)	349.0	24	964.7	18	38.2	74	69.0	131	10.9	7.8	33.1	7	2.16
Compaq Computer	667.7	55	2065.6	69	91.9	88	255.2	87	13.8	11.3	31.3	11	6.30
Control Data	933.0	1	3628.3	8	-12.8	NM	1.7	-93	NM	1.9	0.1	NM	0.03
Cray Research	330.9	102	756.3	10	88.5	160	156.6	6	26.8	20.8	22.9	12	4.99
Data General (3)	308.6	-10	1330.5	2	-19.5	NM	-48.9	NM	NM	4.0	-8.1	NM	-1.72
Digital Equipment (6)	3179.5	14	12284.7	18	279.6	-15	1209.1	-6	8.8	11.8	15.6	12	9.31
Hewlett-Packard (2)	2709.0	19	9831.0	22	243.0	11	816.0	27	9.0	9.6	18.0	16	3.36
International Business Machines	20002.0	9	59681.0	8	2347.0	12	5491.0	4	11.7	11.4	13.9	13	9.27
NCR	1804.2	-1	5989.9	6	149.6	-7	439.3	5	8.3	8.9	19.6	11	5.33
Prime Computer	431.1	61	1594.6	66	-14.4	NM	13.0	-80	NM	8.0	2.4	49	0.39
Sun Microsystems (6)	448.3	91	1461.6	93	29.5	111	89.6	87	6.6	5.9	22.3	15	1.11
Tandem Computers (3)	392.3	39	1424.7	31	31.3	32	102.1	0	8.0	8.4	11.4	18	1.01
Tandy (6)	1402.7	8	3992.3	9	135.0	3	321.3	11	9.6	10.0	18.9	12	3.59
Unisys	2873.9	3	9902.0	2	218.0	1	680.6	18	7.6	7.7	17.2	8	3.58
Wang Laboratories (6)	760.7	-3	3074.5	1	1.0	-97	50.2	-47	0.1	4.3	3.2	31	0.3
Xerox†	4395.7	6	16440.9	9	-77.2	NM	387.8	-33	NM	3.7	6.5	18	3.56
Zenith Electronics	840.7	23	2685.7	14	14.0	198	5.3	NM	1.7	0.7	1.1	NM	0.20
(c) COMPUTER SOFTWARE & SERVICES													
GROUP COMPOSITE	3883.0	19	14240.0	24	302.2	4	970.7	11	7.8	8.9	18.4	17	1.86
AM International (5)	191.5	1	822.6	8	3.7	-58	3.1	-88	1.9	4.6	-1.6	NM	-0.01
Comdisco (3)	374.0**	14	1356.0	10	23.0	-4	91.0	15	6.1	7.3	20.2	11	2.11
Computer Associates Intl. (9)	309.4	59	925.3	43	62.7	47	142.4	70	20.3	21.9	27.0	20	1.89
Computer Sciences (9)	345.5	20	1253.4	11	12.0	16	49.5	22	3.5	3.6	12.9	16	3.11
Continental Information Sys. (10)	196.9	29	772.4	86	-5.3	NM	-10.8	NM	NM	3.7	-19.2	NM	-0.81
Electronic Data Systems	1301.0**	10	4844.1	9	103.4	-1	384.1	19	7.9	8.8	29.1	14	3.11
First Financial Management	141.3**	54	423.7	142	10.1	127	29.3	152	7.1	4.8	12.0	14	1.81
Intergraph	214.8	10	800.2	25	25.0	1	88.0	26	11.6	12.7	13.9	13	1.51
Microsoft (6)	209.9	35	718.6	57	47.5	34	151.4	63	22.6	22.7	32.5	22	2.71
Seagate Technology (6)	340.3	2	1351.0	26	7.6	-67	-5.5	NM	2.2	6.9	-1.4	NM	-0.11
Western Digital (6)	258.4	61	972.9	70	12.7	54	48.3	11	4.9	5.1	16.6	7	1.71
19 PAPER & FOREST PRODUCTS													
INDUSTRY COMPOSITE	17223.3	12	66817.5	16	1288.1	31	5056.1	45	7.5	6.4	17.2	8	4.21
(a) FOREST PRODUCTS													
GROUP COMPOSITE	4630.8	9	18125.0	12	310.6	18	1181.8	32	6.7	6.2	15.4	8	3.51
Boise Cascade	1034.8	6	4094.6	7	76.4	34	289.1	58	7.4	5.9	17.8	7	6.31
Louisiana-Pacific	448.3	8	1799.4	9	31.2	4	135.2	14	7.0	7.2	11.9	9	3.51
Pope & Talbot	142.0	33	515.0	21	8.6	20	31.9	14	6.1	6.7	20.5	7	2.61
Weyerhaeuser	2560.0	9	10000.0	13	154.9	20	564.4	26	6.0	5.5	14.1	10	2.61
Willamette Industries	445.7	17	1716.0	20	39.4	2	161.1	33	8.8	10.2	21.6	7	6.31
(b) PAPER													
GROUP COMPOSITE	12592.6	13	48692.5	17	977.5	36	3874.3	50	7.8	6.4	17.8	8	4.51
APL (3)	259.6	-13	1169.9	133	-6.2	NM	-34.9	NM	NM	NM	-77.6	NA	-9.31
Bowater	367.3	5	1410.4	15	45.5	54	164.3	103	12.4	8.5	19.7	6	4.31
Champion International	1314.4	14	5128.5	11	119.9	46	456.4	19	9.1	7.1	14.1	7	4.81
Chesapeake	176.9	7	711.3	5	15.4	1	51.5	70	8.7	9.2	19.3	8	2.51
Consolidated Papers	222.2	10	896.8	21	36.9	13	149.9	56	16.6	16.1	20.9	10	3.41
Glatfelter (P. H.)	144.1	13	569.3	34	23.2	53	82.2	49	16.1	11.9	25.9	12	3.41
Great Northern Nekoosa	949.6	21	3588.1	39	85.8	51	341.7	70	9.0	7.2	22.3	7	6.21
International Paper	2500.0	24	9535.0	23	206.0	65	754.0	85	8.2	6.2	16.4	7	6.51
James River Corp. of Virginia (8)	1454.6	13	5474.8	16	65.6	23	230.1	22	4.5	4.2	10.8	11	2.51
Kimberly-Clark	1400.0	8	5400.0	10	94.7	15	378.6	16	6.8	6.3	21.4	13	4.71
Mead	1044.6	-2	4463.9	6	54.8	58	364.1	67	5.2	3.3	23.8	7	5.51
Pentair	221.1	12	823.3	4	11.0	3	39.8	82	5.0	5.4	17.9	8	3.71
Scott Paper	1285.4	17	4726.4	15	80.9	20	400.9	71	6.3	6.1	21.8	8	5.11
Union Camp	685.6	9	2660.9	13	78.5	33	295.1	42	11.4	9.4	19.8	8	4.11
Westvaco (2)	567.0	9	2133.9	12	65.8	11	200.4	37	11.6	11.4	15.2	9	3.11

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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12-31	PRICE EARNINGS RATIO 2-28	12 MONTHS' EARNINGS PER SHARE
	4th QUARTER 1988 \$ MIL	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL	CHANGE FROM 1987 %	4th QUARTER 1988 \$ MIL	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL	CHANGE FROM 1987 %	4th QUARTER 1988 %	4th QUARTER 1987 %			
PUBLISHING & BROADCASTING													
INDUSTRY COMPOSITE	11046.7	5	41103.3	9	840.3	18	3438.6	25	7.6	6.8	18.1	19	2.47
BROADCASTING GROUP COMPOSITE	2655.4	1	9621.5	8	194.2	66	617.8	81	7.3	4.4	9.5	30	2.69
American TV & Communications	212.1	13	811.9	14	22.5	72	70.4	42	10.6	7.0	29.4	54	0.65
Capital Cities/ABC	1315.6	-7	4773.4	8	140.2	20	387.1	39	10.7	8.3	13.4	16	22.31
CBS	772.3	0	2777.7	1	40.1	78	283.4	108	5.2	2.9	12.3	15	11.02
Viacom	355.4	34	1258.5	25	-8.6	NM	-123.1	NM	NM	NM	-51.3	NM	-3.54
PUBLISHING GROUP COMPOSITE	8391.3	7	31481.8	9	646.1	9	2820.8	17	7.7	7.5	22.0	17	2.43
Commerce Clearing House	148.8**	12	625.1	11	1.6	-76	49.5	-6	1.1	5.0	22.6	19	2.75
Dow Jones	413.0	-1	1603.1	22	43.1	-14	228.2	12	10.4	12.1	23.2	13	2.35
Dun & Bradstreet	1132.4	11	4267.4	13	123.1	18	499.0	14	10.9	10.2	24.6	20	2.67
Gannett	905.3	8	3314.5	8	117.8	11	364.5	14	13.0	12.8	21.4	16	2.26
Harcourt Brace Jovanovich	253.3	14	1268.1	15	-53.8	NM	-53.5	NM	NM	NM	NM	NM	-2.04
Knight-Ridder	574.6	9	2083.3	6	42.0	-13	146.8	-1	7.3	9.1	16.5	18	2.59
McGraw-Hill	507.4	2	1818.0	4	55.0	10	185.5	13	10.8	10.0	20.9	17	3.83
Media General	191.4**	4	755.7	6	-29.6	NM	8.8	-79	NM	6.2	3.5	NM	0.31
Meredith (6)	195.9	12	746.6	19	10.4	-29	31.8	-31	5.3	8.4	8.5	19	1.66
New York Times	450.0	3	1700.0	4	48.5	17	161.0	3	10.8	9.5	19.5	14	2.00
Scripps (E. W.)	335.7	6	1214.5	6	22.5	NM	70.1	55	6.7	NM	11.5	20	0.93
Time	1207.0	6	4507.0	7	58.0	12	289.0	16	4.8	4.6	21.4	21	5.01
Times Mirror	925.1**	7	3332.6	6	96.8	77	331.9	25	10.5	6.3	20.7	13	2.58
Tribune	624.7	8	2334.8	9	62.9	46	210.4	49	10.1	7.4	18.0	14	2.78
Washington Post	370.8	2	1367.6	4	36.9	-43	269.1	44	10.0	17.6	32.4	10	20.91
Western Publishing Group (11)	155.8**	15	543.3	29	11.0	21	28.9	71	7.1	6.7	18.1	12	1.42
SERVICE INDUSTRIES													
INDUSTRY COMPOSITE	14342.7	18	51646.0	18	430.3	-11	1917.0	20	3.0	4.0	13.4	21	1.37
CONSTRUCTION & ENGINEERING GROUP COMPOSITE	5184.9	15	18592.9	16	-110.8	NM	-71.9	NM	NM	1.3	-2.3	NM	-0.28
Atkinson (G. F.)	254.0	-2	920.0	-5	0.6	NM	1.0	-53	0.2	NM	0.6	NM	0.12
Butler Mfg.	173.1	3	645.6	5	3.9	NM	15.3	400	2.2	NM	12.8	11	3.41
CDI	200.2	30	734.2	32	4.2	44	16.0	47	2.1	1.9	18.2	13	1.68
Combustion Engineering	922.9	3	3483.9	15	-182.3	NM	-245.2	NM	NM	2.0	-31.2	NM	-6.40
CRS Sirtine (6)	155.8	58	608.4	73	2.6	107	9.2	NM	1.7	1.3	13.6	19	1.52
EG&G	386.2	19	1406.3	11	18.4	24	68.7	19	4.8	4.5	23.8	13	2.30
Fischbach (3)	193.6	-15	895.8	-15	-2.8	NM	-20.8	NM	NM	1.8	-21.2	NM	-5.33
Fluor (2)	1605.6	32	5132.5	31	23.6	-2	56.4	NM	1.5	2.0	9.4	32	0.71
Foster Wheeler	305.1	-7	1053.8	-14	7.5	NM	28.5	846	2.5	NM	6.5	21	0.81
Jacobs Engineering Group (3)	165.3	-20	716.3	57	2.1	24	7.0	49	1.2	0.8	13.7	17	1.41
MMR Holding (6)	154.4	24	586.3	42	1.9	-15	8.7	25	1.2	1.8	24.1	11	1.62
Morrison Knudsen	518.5	23	1909.3	10	3.4	-40	-37.0	NM	0.7	1.3	-14.5	NM	-3.35
Thermo Electron	150.3	52	500.6	31	6.1	22	20.1	11	4.1	5.1	11.7	19	1.15
INDUSTRIAL DISTRIBUTION GROUP COMPOSITE	2850.7	8	11406.7	11	129.8	16	503.4	31	4.6	4.2	17.1	15	2.19
Avnet (6)	495.4	15	1933.6	16	11.8	-8	50.7	36	2.4	3.0	7.1	15	1.42
Bearings (6)	153.3	16	582.4	14	4.3	19	16.5	76	2.8	2.8	12.7	11	3.23
Genuine Parts	716.5	11	2942.0	13	49.2	21	181.4	22	6.9	6.3	21.8	15	2.35
Getty Petroleum (11)	221.9	-33	1082.0	-13	6.6	38	26.6	182	3.0	1.4	26.9	8	2.31
Grainger (W. W.)	384.5	14	1535.5	16	25.9	8	108.8	20	6.7	7.1	17.2	14	3.92
Premier Industrial (7)	145.5	14	565.6	16	17.3	11	68.3	22	11.9	12.2	33.8	18	1.59
United Stationers (4)	248.8	18	893.9	17	7.2	24	24.6	49	2.9	2.8	15.6	15	1.59
Univar (10)	328.8	16	1264.9	15	5.2	131	17.9	135	1.6	0.8	16.1	12	2.03
VWR (10)	155.9	9	606.8	12	2.4	19	8.8	6	1.5	1.4	13.1	13	1.60
POLLUTION CONTROL GROUP COMPOSITE	2318.4	33	8082.9	25	235.3	42	852.3	37	10.1	9.5	20.3	20	1.66
Browning-Ferris Industries (3)	583.2	22	2171.8	23	59.6	17	235.7	28	10.2	10.6	21.7	18	1.57
Chemical Waste Management	217.8	42	700.2	25	35.1	49	116.9	35	16.1	15.4	22.3	23	1.17
RC Holding (2)	147.2	62	440.6	18	3.1	NM	-7.1	NM	2.1	NM	NM	NA	NA
Waste Management	972.6	28	3565.6	29	124.7	41	464.2	42	12.8	11.6	22.5	20	2.05
Wheelabrator Technologies	397.5	52	1204.7	20	12.7	91	42.6	70	3.2	2.5	8.4	24	1.07
PRINTING & ADVERTISING GROUP COMPOSITE	1921.6	14	6382.7	15	117.2	8	329.1	-3	6.1	6.4	16.3	14	2.17
Advo-System (3)	153.0	3	593.0	8	-1.6	NM	-8.5	NM	NM	1.9	-27.0	NM	-0.78
Donnelley (R. R.) & Sons	880.3	14	2878.4	16	64.5	13	205.3	-6	7.3	7.4	15.8	14	2.64
Interpublic Group	397.9**	32	1191.9	23	23.3	25	60.1	22	5.9	6.2	20.0	14	2.72
Ogilvy Group	242.4	10	838.1	13	15.4	7	32.9	11	6.4	6.6	18.0	14	2.25
Omnicom Group	248.0	0	881.3	9	15.6	3	39.2	13	6.3	6.1	19.5	13	1.58

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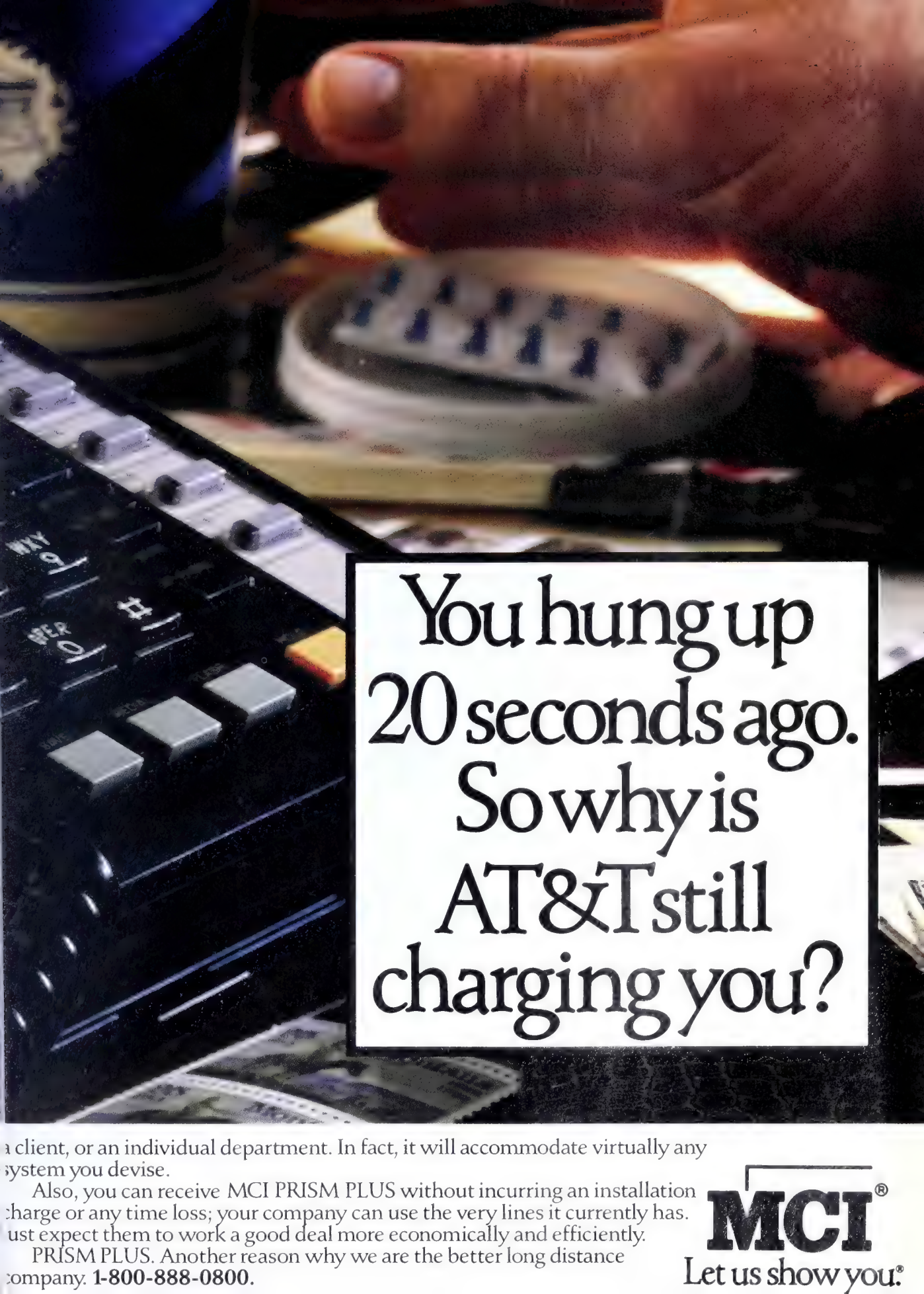


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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12/31	PRICE- EARNINGS RATIO 2/28	12 MONTHS' EARNINGS PER SHARE	
	4th QUARTER 1988 \$ MIL.	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL.	CHANGE FROM 1987 %	4th QUARTER 1988 \$ MIL.	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL.	CHANGE FROM 1987 %	4th QUARTER 1988 %	4th QUARTER 1987 %				
(e) OTHER SERVICES														
GROUP COMPOSITE	2067.2	34	7180.8	26	58.7	53	304.1	34	2.8	2.5	15.5	14	1.21	
Amer. Building Maintenance (2)	153.5	11	581.7	10	2.4	42	7.1	44	1.6	1.2	11.5	16	1.85	
Commtron (4)	169.0**	36	520.2	22	3.0	116	5.4	205	1.8	1.1	11.0	10	0.53	
Handleman (8)	174.2	17	580.0	18	11.0	21	36.0	25	6.3	6.1	21.3	11	2.16	
JWP	316.1	65	925.0	45	8.0	31	27.8	25	2.5	3.2	20.0	12	2.22	
Kelly Services	322.1	3	1269.4	9	14.5	7	60.3	20	4.5	4.4	27.6	14	2.51	
Kinder Care	282.7**	223	935.4	85	0.3	NM	43.3	64	0.1	NM	11.0	10	0.80	
National Education	144.4	18	457.5	15	19.1	NM	46.1	NM	13.2	NM	29.8	16	1.57	
Olsten	142.1	19	516.0	26	4.9	26	17.3	32	3.5	3.3	23.9	18	1.40	
Science Applications (11)	222.7**	25	828.9	29	6.9	15	24.2	20	3.1	3.4	16.0	NA	0.53	
Service Corp. International (8)†	140.4	14	566.8	17	-11.4	NM	36.7	-39	NM	12.7	6.5	22	0.77	
22 TELECOMMUNICATIONS														
INDUSTRY COMPOSITE	38202.4	9	146606.2	5	-476.8	NM	9849.1	-25	NM	8.5	15.7	17	2.37	
(a) EQUIPMENT & SERVICES														
GROUP COMPOSITE	4724.3	34	17323.4	39	261.0	74	1029.4	136	5.5	2.2	21.7	18	1.79	
Alltel	274.5	7	1068.5	8	19.1	-49	125.0	2	7.0	14.4	15.7	13	2.91	
Contel	848.9	11	2963.7	8	72.8	NM	311.6	262	8.6	NM	20.2	12	3.95	
LPL Investment Group	150.6	18	585.4	69	4.0	71	9.3	81	2.7	1.8	19.1	11	1.34	
MCI Communications	1431.0	38	5137.0	30	132.0	257	356.0	356	9.2	3.6	28.1	19	1.27	
Pacific Telecom	142.6	7	552.1	5	15.0	-4	58.4	31	10.5	11.7	13.0	13	1.52	
Telecom-USA	143.2	33	523.7	32	7.4	93	27.3	82	5.2	3.6	47.1	18	1.07	
United Telecommunications	1733.6	122	6493.0	121	10.7	NM	141.8	NM	0.6	4.2	9.0	36	1.36	
(b) TELEPHONE COMPANIES														
GROUP COMPOSITE	33478.1	5	129282.8	5	-737.8	NM	8819.7	-26	NM	9.1	9.9	17	2.47	
Ameritech	2504.4	2	9903.3	4	309.7	-4	1237.4	4	12.4	13.2	15.8	11	4.55	
American Telephone & Telegraph	9207.0	6	35210.0	4	-3342.0	NM	-1669.0	NM	NM	5.8	-11.0	NM	-1.55	
Bell Atlantic	2771.6	2	10880.1	1	302.6	6	1316.8	6	10.9	10.5	14.3	11	6.65	
BellSouth	3577.2	13	13596.9	11	419.3	2	1665.5	0	11.7	13.0	14.1	12	3.51	
Centel	284.3	4	1094.9	2	21.2	-34	109.8	-18	7.4	11.7	11.9	24	2.60	
Cincinnati Bell	195.2	11	738.4	16	17.3	-3	84.3	31	8.9	10.2	17.0	16	2.63	
GTE	4309.2	6	16459.8	7	326.2	-2	1224.7	9	7.6	8.2	14.5	12	3.58	
Nynex	3243.0	5	12660.8	5	342.2	6	1315.0	3	10.6	10.4	14.0	10	6.63	
Pacific Telesis Group	2428.0	1	9483.0	4	249.0	66	1188.0	25	10.3	6.2	14.7	12	2.81	
Southern New England Tel.	423.4**	7	1582.6	6	39.8	10	155.4	11	9.4	9.2	13.7	13	4.99	
Southwestern Bell	2186.2	2	8452.7	6	305.2	24	1060.1	1	14.0	11.5	12.6	12	3.53	
US West	2348.7	1	9220.6	6	271.7	7	1131.7	13	11.6	11.0	14.5	10	6.17	
23 TRANSPORTATION														
INDUSTRY COMPOSITE	28454.9	12	109693.3	14	1053.7	236	3759.9	49	3.7	1.2	9.0	15	2.19	
(a) AIRLINES														
GROUP COMPOSITE	12841.8	12	51079.3	17	48.9	NM	989.0	NM	0.4	NM	8.8	16	2.10	
Alaska Air Group	196.5	12	814.4	15	6.1	984	37.5	181	3.1	0.3	12.4	10	2.37	
America West Airlines	211.8	29	775.7	35	2.5	NM	-12.2	NM	1.2	NM	-36.5	NM	-0.92	
AMR	2368.0	26	8824.3	23	116.7	NM	476.8	140	4.9	NM	15.4	7	7.92	
Delta Air Lines (6)	1858.1	9	7323.4	15	85.2	-4	344.5	48	4.6	5.2	15.0	8	7.02	
NWA	1418.3	17	5650.4	10	34.0	NM	135.1	31	2.4	0.0	8.4	15	4.63	
Pan Am	839.9	11	3569.0	17	-55.4	NM	-96.9	NM	NM	NM	NM	NM	-0.68	
Southwest Airlines	225.8	16	860.4	11	16.1	80	58.0	188	7.1	4.6	10.5	13	1.84	
Texas Air	2018.5	-5	8572.9	-1	-224.4	NM	-718.6	NM	NM	NM	NM	NM	-18.88	
UAL	2221.9	6	8981.7	8	45.4	NM	599.9	NM	2.0	NM	50.0	6	20.20	
USAir Group	1482.9	32	5707.0	90	22.8	-15	165.0	-15	1.5	2.4	8.1	10	3.81	
(b) RAILROADS														
GROUP COMPOSITE	8008.4	10	30448.2	10	748.2	23	1884.9	8	9.3	8.4	8.2	15	2.46	
Burlington Northern	1181.4	7	4699.5	11	43.0	-6	207.2	16	3.6	4.1	5.7	9	2.76	
CNW	247.6	7	995.5	11	43.5	NM	69.3	323	17.6	NM	12.8	9	3.71	
Consolidated Rail	904.0	8	3490.0	7	78.0	-1	306.0	15	8.6	9.4	7.7	8	4.44	
CSX	2048.0	11	7592.0	9	126.0	10	-38.0	NM	6.2	6.3	-1.0	NM	-0.33	
Norfolk Southern	1160.0	9	4460.0	9	179.0	3	635.0	268	15.4	16.3	12.6	10	3.51	
Santa Fe Southern Pacific	885.3	9	3143.6	11	122.7	51	146.7	-39	13.9	10.0	45.0	26	0.93	
Union Pacific	1582.1	15	6067.6	13	156.0	32	558.7	13	9.9	8.6	12.5	14	4.90	
(c) TRANSPORTATION SERVICES														
GROUP COMPOSITE	4483.0	10	17236.6	11	117.4	10	389.9	-14	2.6	2.6	9.1	20	1.33	
Airborne Freight	209.9	23	768.0	21	1.7	1	7.0	19	0.8	1.0	5.6	22	1.01	
Avondale Industries	160.6	25	570.3	9	4.8	43	9.1	-14	3.0	2.6	3.6	31	0.59	
Emery Air Freight	313.9	12	1270.1	4	-15.7	NM	-51.1	NM	NM	NM	-44.2	NM	-2.21	
Federal Express (7)	1136.1	20	4244.5	21	52.5	19	192.0	9	4.6	4.7	13.7	14	3.67	

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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY 12 MONTHS ENDING 12/31	PRICE- EARNINGS RATIO 2/28	12 MONTHS EARNING PER SHARE
	4th QUARTER 1988 \$ MIL.	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL.	CHANGE FROM 1987 %	4th QUARTER 1988 \$ MIL.	CHANGE FROM 1987 %	12 MONTHS 1988 \$ MIL.	CHANGE FROM 1987 %	4th QUARTER 1988 %	4th QUARTER 1987 %			
Gatx	157.7**	9	587.1	7	9.0	11	47.0	-35	5.7	5.6	20.7	11	5.04
PHH (8)	423.6	15	1736.3	21	10.5	4	19.6	-54	2.5	2.7	5.9	28	1.18
Ryder System	1313.4	8	5029.6	9	47.9	5	134.7	-28	3.6	3.8	9.0	16	1.61
Subaru of America (2)	397.0	5	1673.2	-6	-26.1	NM	-57.9	NM	NM	NM	-27.6	NM	-1.19
Tiger International	370.7	5	1357.5	10	32.8	22	89.5	24	8.9	7.6	73.1	9	2.36
(d) TRUCKING & SHIPPING GROUP COMPOSITE	3121.7	16	10929.8	15	139.2	58	496.1	32	4.5	3.3	14.8	12	2.56
Alexander & Baldwin	161.9	0	664.5	5	26.8	18	135.1	12	16.6	14.1	23.1	13	2.70
American President	618.5**	22	2131.2	17	15.5	9	81.3	3	2.5	2.8	10.9	10	3.46
Carolina Freight	207.3	8	650.2	9	5.1	363	10.0	15	2.5	0.6	7.8	16	1.50
Consolidated Freightways	717.5	16	2689.1	17	40.3	96	113.2	52	5.6	3.3	15.4	10	3.00
Preston	151.3	12	593.7	17	0.8	NM	7.3	NM	0.6	NM	6.5	12	1.27
Roadway Services	741.6	21	2184.5	14	31.8	70	80.2	59	4.3	3.0	12.0	16	2.00
Yellow Freight System	523.7	14	2016.5	15	18.8	65	69.0	67	3.6	2.5	16.9	12	2.40
24 UTILITIES													
INDUSTRY COMPOSITE	47006.1	5	185773.4	5	1758.4	-49	16778.5	-10	3.7	7.7	10.3	11	2.19
(a) ELECTRIC GROUP COMPOSITE	34719.5	7	141646.1	5	1333.1	-55	15259.9	-11	3.8	9.0	10.6	11	2.29
Allegheny Power System	524.9	-1	2170.5	10	56.0	10	223.6	-1	10.7	9.6	13.6	9	3.96
American Electric Power	1232.0	7	4840.8	1	176.8	64	693.3	19	14.4	9.4	15.0	8	3.24
Atlantic Energy	162.4	12	675.8	4	11.1	5	76.7	-2	6.8	7.3	13.3	9	3.68
Baltimore Gas & Electric	426.4	10	1863.7	3	43.9	-10	303.4	1	10.3	12.5	14.5	9	3.47
Boston Edison	279.3	-7	1202.7	2	16.7	110	84.2	-3	6.0	2.7	9.6	9	1.86
Carolina Power & Light	561.3	11	2273.4	9	43.7	-36	196.8	-44	7.8	13.4	7.1	17	2.04
Centenier Energy	461.3	13	2037.6	6	-310.6	NM	-32.6	NM	NM	20.1	-3.7	NM	-0.73
Central & South West	569.0	0	2512.0	3	35.0	-57	356.0	-11	6.2	14.4	12.5	9	3.43
Central Maine Power	179.0	7	653.7	4	4.1	-69	45.8	-1	2.3	8.0	11.7	10	1.83
Cincinnati Gas & Electric	364.9	6	1385.9	2	46.9	NM	226.9	99	12.9	NM	18.0	6	4.32
CMS Energy	860.5	8	2942.7	6	79.2	-17	296.3	-8	9.2	11.9	17.1	7	3.31
Commonwealth Edison	1349.5	10	5613.3	-1	74.8	-59	737.5	-32	5.5	14.9	9.0	11	3.01
Commonwealth Energy System	180.8	5	677.0	3	13.1	34	35.0	8	7.2	5.6	11.7	9	3.50
Consolidated Edison Co. of N. Y.	1211.5	2	5108.8	0	94.2	54	599.3	9	7.8	5.1	13.3	9	4.93
Delmarva Power & Light	176.8	7	768.3	8	9.8	93	84.7	6	5.6	3.1	12.7	10	1.70
Detroit Edison	760.7	13	3102.2	9	-462.4	NM	-235.3	NM	NM	15.9	-10.3	NM	-1.94
Dominion Resources	863.6**	13	3358.9	3	103.4	6	489.7	2	12.0	12.7	13.7	9	4.52
DPL	263.0	6	988.7	5	20.4	NM	135.7	34	7.8	NM	14.7	8	3.01
Duke Power	850.2	-5	3627.0	-2	24.2	-74	448.1	-10	2.9	10.3	11.5	11	3.90
Duquesne Light	277.2	27	1063.2	20	34.5	-24	137.4	-11	12.5	20.6	10.7	10	1.86
Florida Progress	472.8	-2	2002.0	2	38.5	14	196.6	-5	8.1	7.0	13.7	10	3.52
FPL Group	1391.7	26	5853.5	32	97.0	17	493.3	9	7.0	7.6	13.7	9	3.42
General Public Utilities	672.8	7	2834.0	6	42.5	-24	313.8	8	6.3	8.8	14.0	8	4.75
Gulf States Utilities	366.8	9	1520.5	6	7.6	-84	103.1	-57	2.1	14.2	1.9	23	0.37
Hawaiian Electric Industries	194.0	18	733.1	15	13.3	317	59.7	40	6.8	1.9	12.4	10	2.90
Illinois Power	288.2	-1	1284.7	5	5.9	-86	155.4	-46	2.0	13.9	6.2	10	1.66
Kansas City Power & Light	159.6	2	736.5	4	6.4	-54	105.7	2	4.0	8.9	12.0	9	3.20
Kansas Power & Light	262.6	-14	1166.1	0	12.5	-35	79.8	-10	4.8	6.3	12.9	10	2.25
Long Island Lighting	480.3	1	2137.8	3	16.8	-68	298.5	11	3.5	11.0	8.9	7	2.02
Louisville Gas & Electric	154.7	12	659.7	5	10.5	23	85.0	12	6.8	6.1	13.1	9	3.70
Middle South Utilities	863.5	11	3565.4	3	79.9	NM	498.0	11	9.3	NM	8.5	8	2.01
Midwest Energy	152.5	-1	570.3	6	10.0	-19	43.9	17	6.6	8.1	14.7	10	1.83
New England Electric System	370.8	9	1519.7	5	22.7	-49	-43.2	NM	6.1	13.0	-5.1	NM	-0.94
New York State Electric & Gas	336.2	13	1340.2	4	25.2	NM	171.5	228	7.5	NM	13.5	8	2.81
Niagara Mohawk Power	678.9	4	2800.5	7	-3.8	NM	208.8	261	NM	NM	8.5	10	1.21
Nipsco Industries	425.5	8	1524.2	5	39.3	176	122.9	89	9.2	3.6	10.1	10	1.41
Northeast Utilities	528.0	8	2079.2	11	68.1	87	263.4	4	12.9	7.5	12.2	9	2.07
Northern States Power	483.9	13	2006.5	13	22.3	-23	214.8	5	4.6	6.7	13.6	10	3.11
Ohio Edison	533.0	28	2142.6	20	99.1	31	357.5	-16	18.6	18.1	11.9	10	2.06
Oklahoma Gas & Electric	232.5	3	1098.2	3	16.2	-37	137.8	21	7.0	11.4	15.2	10	3.20
Pacific Gas & Electric	2043.6	12	7645.7	6	-461.6	NM	62.1	-90	NM	8.1	-0.5	NM	-0.10
PacifiCorp	931.7	9	3519.3	7	105.9	-9	446.7	9	11.4	13.6	23.1	10	3.46
Pennsylvania Power & Light	552.1	0	2213.9	6	75.8	-1	332.0	10	13.7	13.8	13.7	9	3.73
Philadelphia Electric	778.8	6	3228.7	1	97.7	-20	565.9	5	12.5	16.6	13.0	8	2.33
Pinnacle West Capital	322.8	5	1442.0	9	-125.7	NM	4.2	-98	NM	18.7	NA	NM	0.05
Portland General	211.4	4	762.2	0	42.5	179	109.4	14	20.1	7.5	11.3	11	2.11
Potomac Electric Power	278.9	2	1349.8	1	33.3	5	211.1	1	11.9	11.5	16.2	9	2.14
PSI Holdings	256.6	-3	1043.3	-3	-2.3	NM	114.4	-21	NM	13.0	21.5	7	1.84
Public Service Co. of Colorado	413.9	-1	1685.3	2	50.4	43	125.0	-13	12.2	8.4	13.0	10	2.14
Public Service of New Hampshire	152.9	4	603.5	10	13.2	NM	55.3	NM	8.6	NM	18.6	4	1.14
Public Service Enterprise Group	1154.5	11	4394.7	4	91.6	7	559.9	0	7.9	8.2	13.5	9	2.57
Puget Sound Power & Light	227.2	12	791.4	9	34.9	7	128.2	6	15.3	16.0	13.2	9	2.14
Rochester Gas & Electric	197.9	11	774.0	6	10.6	NM	76.1	213	5.3	NM	12.6	8	2.25
San Diego Gas & Electric	525.9	-1	2076.1	9	47.4	-5	189.4	6	9.0	9.4	14.4	12	3.18
Scana	270.1	7	1083.3	-3	23.7	27	128.8	-8	8.8	7.4	13.4	10	3.06
SCFcorp	1437.0	3	5931.7	8	118.0	-35	808.5	12	8.2	13.1	15.0	9	3.45

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CORPORATE SCOREBOARD

COMPANY	SALES				PROFITS				MARGINS		RETURN ON COMMON EQUITY		PER SHARE EARNINGS	
	1997	1996	1995	1994	1997	1996	1995	1994	1997	1996	1997	1996	1997	1996
	\$ MIL.	\$ MIL.	\$ MIL.	\$ MIL.	\$ MIL.	\$ MIL.	\$ MIL.	\$ MIL.	%	%	%	%	\$	\$
Southern	644.0	0	706.2	1	176.3	72	96.8	38	10.8	6.3	12.7	9	2.17	
Southwestern Public Service	184.0	-2	790.9	2	23.3	-18	104.9	1	12.7	15.1	15.6	11	2.38	
Teco Energy	149.5	5	1034.0	2	23.3	20	136.1	6	9.3	8.0	14.6	11	2.13	
Texas Utilities	184.4	0	4153.7	1	126.1	-20	737.6	-44	13.1	16.7	11.4	7	4.00	
Union Electric	422.2	0	2009.1	4	30.1	-39	291.6	-13	5.2	8.6	13.6	9	2.56	
Utilicorp United	166.9	6	671.6	10	10.7	14	40.9	23	5.7	5.3	12.1	9	1.94	
Wisconsin Energy	401.8	13	1540.7	13	22.0	-47	189.1	6	5.5	11.6	14.9	10	2.73	
Wisconsin Public Service	160.6	3	264.3	4	14.6	0	56.4	7	9.0	9.3	14.0	9	2.28	
WPL Holdings	166.7	10	600.9	9	10.6	-22	61.7	6	8.7	12.2	13.9	10	2.18	
GAS & TRANSMISSION GROUP COMPOSITE	12286.6	2	44127.9	2	425.3	-11	1518.6	-4	3.5	4.0	7.8	19	1.55	
Arkla	541.3	5	1995.8	4	40.1	10	124.8	6	7.8	7.4	16.7	13	1.39	
Atlanta Gas Light	196.6	-1	973.5	-6	16.5	-12	46.7	-15	5.6	6.4	11.1	12	2.07	
Brooklyn Union Gas	297.8	11	927.6	3	31.2	21	67.1	13	10.6	9.6	13.3	9	2.70	
Columbia Gas System	690.6	-10	3126.9	12	53.1	46	119.3	0	6.0	4.0	7.3	14	2.46	
Consolidated Natural Gas	789.9	16	2467.8	6	63.2	-49	192.9	4	8.0	10.2	12.0	16	2.34	
Diversified Energies	211.9	15	766.9	17	7.0	-30	32.3	14	3.3	5.4	13.0	12	2.00	
Eastern Gas & Fuel Associates	174.6	0	671.9	-1	16.6	18	50.7	7	9.6	8.1	10.9	11	2.16	
Enron	1461.0	1	5766.0	-4	27.9	NM	130.2	143	1.9	0.1	6.6	19	1.99	
Enserch	711.7	5	2726.6	7	7.8	-53	10.7	-83	1.1	2.4	-0.7	NM	-0.07	
Laclede Gas	107.6	2	465.6	9	7.3	-5	24.4	7	5.7	6.1	13.3	10	3.10	
MCN	396.1	18	1281.3	3	16.0	17	49.4	1	4.0	4.0	19.2	13	1.16	
National Fuel Gas	251.5	18	766.1	9	19.3	29	47.0	27	7.7	6.7	13.0	10	1.81	
Nicor	463.9	4	1604.3	6	37.5	6	106.2	27	8.1	5.2	17.4	9	3.48	
Pacific Enterprises	1569.6	13	5932.1	11	45.9	-15	229.3	-1	2.7	3.6	17.6	12	3.81	
Panhandle Eastern	275.2	-24	1261.6	-19	-31.6	NM	-171.9	NM	NM	9.8	-20.6	NM	-3.13	
Peoples Energy	292.4	6	1133.6	1	24.7	23	82.6	44	6.5	7.3	15.9	8	2.46	
Sonat	363.3	6	1341.4	-2	11.7	-39	84.7	6	3.2	5.5	7.7	14	2.09	
Southwest Gas	429.0	14	3011.5	16	16.5	-44	41.2	9	3.6	4.6	12.9	8	2.19	
Texas Eastern	986.6	7	3461.0	-4	42.3	20	177.0	59	4.3	3.8	12.5	16	3.13	
Transco Energy	667.6	-14	1774.1	-12	-56.6	NM	-27.2	NM	NM	NM	-8.4	NM	-1.97	
Valero Energy	186.3	1	770.6	23	9.9	NM	93.6	-4	5.3	NM	2.8	22	2.64	
Washington Gas Light	231.8	17	698.0	2	21.1	4	45.1	14	9.1	10.2	11.4	10	2.52	
Wicor	212.5	10	754.2	11	12.8	16	33.9	65	6.0	5.7	15.0	8	4.91	
Williams	449.7	-23	1673.1	-6	-16.1	NM	-4.9	NM	NM	NM	-0.4	NM	-0.11	

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COMPAQ PORTABLE 386

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That's one reason Compaq has created the broadest line of Intel 386™-based personal computers available. Each is designed to deliver the highest-performing solution for every

different user's needs, with unmatched industry-standard compatibility and connectivity.

Take the COMPAQ DESKPRO 386/25, for example. For users who require the ultimate in performance, it's the most powerful personal computer available. And with standard features like eight expansion slots, your choice of four different storage devices and a wide selection of graphics

controllers, it's one of the most flexible personal computers, too.

The COMPAQ DESKPRO 386/20e brings the power of a 20-MHz 386 chip to personal computer users who are outgrowing their 286-based PC's.

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COMPAQ DESKPRO 386/20e



COMPAQ DESKPRO 386/25

f personal computers. or the power-hungry.

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CORPORATE SCOREBOARD

ALPHABETICAL LIST OF COMPANIES

The number following each company name identifies the Scoreboard category under which it is listed

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Engelhard 4
Enron 24b
Enserch 24b
Equifax 17a
Essex 18a
Ethyl 4
Exxon 11b

F

Family Dollar Stores 8
Farm House Foods 10a
Federal Express 23c
Fed Natl Mortgage 17a
Federal Paper Board 7b
Federal-Mogul 2b
Ferro 4
FHP International 12c
Fieldcrest Cannon 15d
Figgie International 5
Finevest Foods 10a
Fireman's Fund 17b
First Bank System 3b
First Capital 17b
First Chicago 3b
First City Bancorp 3d
First Financial Mgmt 18c
First Interstate 3b
First of America 3b
First Union 3c
First Wachovia 3c
Fischbach 21a
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Fleming 10a
Florida Progress 24a
Flowers Industries 10b
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FMC 15c
Food Lion 10c
Ford Motor 2a
Foster Wheeler 21a
Foxboro 9c
FPL Group 24a
Freepart-McMoran 4
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Fruit of the Loom 6a
Fuller (H. B.) 4
Fuqua Industries 5

G

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GenCorp 1
General Cinema 6c
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General Electric 5
General Instrument 9b
General Mills 10b
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General Public Utis 24a
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Norton 15a
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Southmark 13b
Southwest Airlines 23a
Southwest Gas 24b
Southwestern Bell 22b
Southwestern P. S. 24a
Sovran Financial 3c
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Standard Fed. Bank 17c
Standard Register 18a
Standard Shares 5
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Stanley Works 15b
Sterling Chemicals 4
Stewart & Stevenson 15c
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Strawbridge & Clothier 8
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FELLHEIMER: "I GUESS PEOPLE FIND ME INTIMIDATING AND SCARY"

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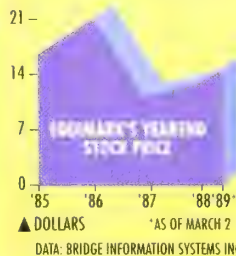
Fixing Equibank gave him a fight he hadn't bargained for

Lawyer Alan S. Fellheimer used to brag that the banking business is simple. "You just collect deposits and lend them out at a nice spread," he complained at a press conference last year. His proof was the dramatic recovery of Equibank Corp., the once-ailing bank holding company he took over in 1985. His job was done, he said. Equibank, the firm's \$3 billion main subsidiary, was officially "fixed" and for sale. Fellheimer, 46, made it look pretty easy—up to a point. In the five years since regulators threatened to shut down Pittsburgh-based Equibank, he shed nonperforming loans from \$120 million to \$33 million, cut staff by 23%, and closed or sold 23 branches. Last year profits climbed to \$5 million, a far cry from the \$58 million in combined losses in 1984 and 1985. His work was nothing short of miraculous," says William M. Mac, former Federal Deposit Insurance Corp. chairman. But Fellheimer has also learned some painful lessons about banking.

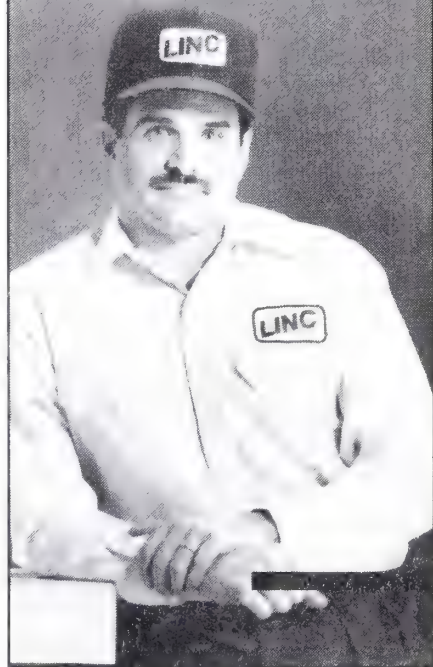
After 10 months on the block, Equibank didn't get one bid. Potential buyers were turned off by a fat asking price—\$250 million, some 75% above its recent market value—for a bank with modest growth potential. In January, Fellheimer announced that "the bank is no longer for sale." Now he has to find a way to keep earnings growing, and Wall Street does not seem overly confident. Equibank's stock rests below book value at around 14—about what it was fetching four years ago (chart). And four major investors, including raider Saul P. Steinberg, have bailed out. To top it off, Fellheimer had to fend off a nasty bid by one investor to have him ousted.

GADFLY BITES. The heat came from David F. Bolger, a small-scale raider who owns an investment firm in Ridgewood, N. J. In early 1988, Bolger, then a director, pushed for the bank's sale. After Labor Day, when no buyers had materialized, he began bombarding directors with letters raising questions about Fellheimer's management. Among other

FELLHEIMER: FEW FANS ON WALL STREET



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things, he charged that Fellheimer made risky loans without proper board approval, used bank-chartered jets for personal trips, and was paid too much money. (He took home a tidy \$1.1 million last year—more than the chief executive officers of Pittsburgh's much larger Mellon Bank and PNC Financial Corp.) EquiMark's board set up a special committee to investigate. Bolger also took his story to state and federal banking regulators.

In one instance, Bolger questioned a \$240,000 loan to a group led by EquiMark Director C. Andrew Russell, a one-time Pittsburgh Steeler who now is chairman of an investment firm. Bolger said that a loan for a small office building renovation was made without sufficient collateral. In another case, Bolger alleged, the bank lent \$13.5 million for a shopping center project without proper disclosure to the board by Fellheimer and a lending officer. The terms of both

Fellheimer has real incentive to get the bank in high gear: He pledged all he owned for his 8.3% stake

loans were later changed to meet the board's policy standards.

Fellheimer denies he did anything wrong. And at his urging, the chairman of the bank's investigative committee recently spent four hours with a reporter detailing how its report cleared Fellheimer of any wrongdoing. The board even probed whether Fellheimer charged the bank for dog food for his bulldog, Sam. Saying that the report was anything but a coverup, J. Bruce Johnston, committee chairman and an executive vice-president of USX Corp., notes: "For a lousy \$9,000 [in director's fees], I'm not going to the slammer for anyone." Regulators also seem satisfied. Officials from the Federal Reserve Bank of Cleveland and the Pennsylvania Banking Dept. told the board they consider the matter closed. Bolger, who sold his stake back to EquiMark last month, declined to comment.

Yet Fellheimer still has his hands full. For the first time in a decade, the bank must pay federal income taxes, which will total about 25% of earnings. In addition, lacking business from Pittsburgh's major corporations, Equibank has aggressively sought small-business loans. During 1986 and 1987, Equibank "took a mix of loans that were very risky," says Leonard M. Matz, former executive vice-president for credit policy. Fellheimer ar-

gues strenuously that the portfolio is sound, however.

Either way, he clearly has had trouble making the transition from hard-nosed Mr. Fixit to the polite world of banking. The normally low-key Ben McInteer, retired Pennsylvania banking commissioner, recalls numerous telephone shouting matches with Fellheimer over his plans for the bank. He hasn't exactly fit into the local social scene, either. Fellheimer admits that he and his team of 20-odd senior managers have been "black-balled" by a number of Pittsburgh country clubs, including the ritzy Longue Vue Club. "I guess people find me intimidating and scary," he says.

Fellheimer's tough-guy style comes straight from the poor Mt. Airy neighborhood in Philadelphia, where his father was a door-to-door salesman. With his family unable to pay for college, he drove a cab to put himself through Temple University and later prepared tax returns to pay for tuition at Temple's law school. He first worked at one Philadelphia firm, then founded a practice with his second wife, Judith. His banking career began in 1980, when he joined investor James D. Lowry in turning around Bank of New Jersey. In 1984, Lowry brought Fellheimer to Equibank to clear up its problem loans. Lowry, the chairman, left the next year in a dispute when the board refused to sell the bank. **WORKAHOLIC.** Like many turnaround specialists, Fellheimer has uncommon stamina. He works long hours, and his subordinates can't keep his frenzied pace, they're gone. He has had three chief financial officers in three years. Price Waterhouse resigned as the bank's auditor in 1987, partly because Fellheimer blamed the firm for messing up his personal checking account.

But Fellheimer also has his share of supporters. "Alan is the single most valuable asset of this bank," says board member Johnston. Equally important is the unconventional team of executive surrounding the chairman: EquiMark's 1.35% level of nonperforming assets is so good because of his stable of well paid collectors—known around headquarters as "kneecappers"—who include a former Israeli tank commander.

With Bolger's allegations behind him, Fellheimer now must concentrate on building the bank. In addition to standard loans, he's also depending on income from investing in—and fixing—other problem banks and thrifts. "If this bank doesn't make it, I don't make it," he says. That's because he pledged everything he owns to buy his 8.3% stake. It was a gutsy move. But back then he still thought banking was simple.

By Michael Schroeder in Pittsburgh

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CAN AVON GET WALL STREET TO ANSWER THE DOOR?

Chairman Preston plans to cut and cut, but doubters abound

When James E. Preston, the new chairman of Avon Products Inc., threw himself a coming-out party on Mar. 7, it was a wonder anyone from Wall Street showed up. Avon stock, selling at half the price fetched 10 years ago, doesn't top any analysts' buy lists. And as Preston was quick to point out, he didn't inherit a lot of credibility. But the 25-year Avon veteran did note the bright side:

"Disastrous acquisitions are behind Avon, sales of beauty products are picking up, and there is even a chance to start chipping away at the company's monstrous debt. This business will be run fundamentally differently than it has been in the past," he vowed.

Encouraging words. But Wall Street didn't rush out to buy Avon. The stock ended the day at 23, unchanged, following Preston's presentation. It'll take a lot more than promises to get investors to forget past appointments.

Preston is tough enough for the assignment. Soon after he became chief executive in September, he bit the bullet and ended a costly diversification into health care engineered by his predecessor, Hicks B. Waldron. Waldron had hoped to build health care into a billion business but abandoned the strategy for Medicare's cost-containment efforts squeezed profits. As Waldron, 65, was preparing to retire, Preston announced a \$425 million reserve to cover

the cost of bailing out of health care. Avon has already sold a home care operation and is trying to unload a retirement-home business and a company that builds health care facilities. Because of the reserve, Avon lost \$405 million last year on sales that rose 18%, to \$3 billion.

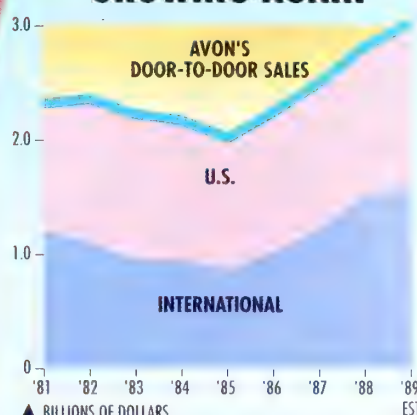
NEW ROLE. Cleansing Avon's balance sheet is Preston's next priority. The company's brief stay in health care helped push debt to \$1.1 billion—a scary 82% of capitalization. Avon's interest costs are expected to hit \$130 million this year. To keep that from growing, Preston has vowed not to make any acquisitions for 18 months. And to ease the existing burden, he launched a major cost-cutting plan in January. The goal: to slash costs by \$100 million by the end of next year.

The company has already cut total employment by 28%, to 28,400, and halved its dividend, to \$1. Now Preston says more staff cuts are likely. Last year, Avon had 25 corporate and beauty group officers. By the end of March they'll number only 13. But most of the savings will come from its U.S. direct sales business, where it plans to shrink both its ad budget and catalog.

For Preston, 55, the role



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The Corporation

of financial manager is a new one. After graduating with a degree in speech from Northwestern University in 1955, he joined the McCann-Erickson Worldwide advertising agency, where he worked on TV and radio ad production. He even did a stint as a movie producer before joining Avon's management training program in 1964. Once at Avon, Preston zipped up through a series of marketing and personnel jobs, landing the top spot at Avon's beauty division in 1981.

His claim to fame: a successful makeover of Avon's beauty operations. The company had ignored the flood of women into the work force, and Avon Ladies began to find their traditional door-to-door sales methods ineffective. Preston persuaded Avon to stop looking at its sales force as its customers and to begin conducting consumer research. Now Avon is introducing products in niches it ignored before. One example: Avon rolled out upscale skin care lines, including a hot seller called BioAdvance.

NIGHTIES, TOO. To get Avon's sales rolling, Preston offered free training to sales representatives, who previously had to pay a fee. He boosted commissions and began rewarding the best producers with more profitable territories. Avon is also following women to work. "More than 50% of my business is generated through offices and corporations," says Terry Engebretson, an Avon Lady in Redwood City, Calif.

Preston says Avon's beauty business is sitting prettier than it has been for years. In 1988 pretax profits of door-to-door operations jumped 10%, to \$388 million. But he acknowledges that the competitive cosmetics market is growing only 2% to 3% a year, with Avon's growth not likely to be much higher. So he is testing door-to-door sales of lingerie, toys, and videotapes.

The company is growing more quickly overseas, especially in Japan, Britain, and Mexico, where it doesn't have as much competition from drug chains. Longer term, Avon is counting on retail distribution to keep growing. It entered the fray at department-store perfume counters with its 1987 acquisitions of Giorgio Inc. and Parfums Stern—for a total of \$325 million.

Early results were disappointing—it's first fragrance, Deneuve, flopped. But prestige perfumes seem to be coming on stronger. Avon launched Cher's Uninhibited perfume last November and followed earlier this year with Red, an addition to the Giorgio line. "Cher looked good, and Red is looking very, very good," says Allan G. Mottus, an industry consultant. Expected next: a line of makeup for department store distribution, perhaps under the Giorgio name.

Avon's complexion isn't trouble free, however. Analysts complain it has too many low-producing sales reps who don't justify their overhead. In fact, customer sales per Avon Lady are expected to increase only about 2% this year, after a small dip in 1988, according to Andrew Shore, a cosmetics analyst with Shearson Lehman Hutton Inc. And if Avon cuts advertising to save money that could eventually hurt sales. Upscale fragrances won't help much, either, generating only about \$300 million in revenues this year and no profits until 1990.

After years of broken promises and strategic reversals, investors are upset.



PRESTON: MAKING THE PRODUCT FIT THE NICH

The California Public Employees Retirement System, for example, bought 375,000 shares of Avon's common stock at \$61 per share and has since converted all but 18,583 shares to Avon preferred. "Their record looks awful in our books," complains Jose Arau, principal investment officer for the system.

If Preston can't boost Avon's share price, he may end up with investors of an even more unfriendly variety. Despite Avon's massive debt, the company has long been rumored as a takeover target. Avon officials say they know of no immediate threat, but suspected raiders include Revlon Inc. and Fabergé Inc.

For now, Preston is fighting the threat by minding Avon's cosmetic business and fighting to pay down about \$100 million of debt this year. It isn't dramatic, but it should be the kind of news Avon's shell-shocked investors are longing to hear. If Preston's debt-reduction plan stays on course, he might even close that credibility gap.

By Kathleen Deveny in New York

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THE MOMMY TRACK

JUGGLING KIDS AND CAREERS IN CORPORATE AMERICA TAKES A CONTROVERSIAL TURN

'You are going to miss out at work. Every once in a while it stings'

ANNE KELLER still hankers for a fast-track marketing job. But full-time work can wait until Cara and Nicholas are both in school. For now, three days a week at Digital Equipment keep Keller in the loop. "I spend Mondays catching up," she says. But the transition between work and home "is hard." Thursdays, she has to "turn it off and get into being a mother." When the kids nap, she calls her office.



On Monday, Tuesday, and Wednesday, Anne Keller, middle manager, is in corporate life. As a marketing analyst at Digital Equipment Corp.'s worldwide headquarters in Stowe, Vt., she is a liaison between the company's far-flung sales and its engineering department. Keller has new-product introductions to follow up on technical work to review. There are memos and meetings. Deadlines. Day care.

When it stops. Thursday morning, as PCs boot up, and fax machines all over America begin humming, you can find Anne Keller, mom, down at the neighborhood diner. She orders eggs and hash browns for her two children, 16-month-old Nicholas and a 4. After breakfast, it's grocery shopping and play dates. She pours countless cups of juice and wipes up spills... until Monday morning, when reality shifts again.

DIFFICULT. "I'm neither fish nor fowl," says Keller. But her kind of life is multiplying. Across the country, female managers and professionals with young families are leaving the fast track for the mommy track. They are searching for new ways to balance career goals and motherhood—a human place to stand, if you will, between Superwoman and June Cleaver. Their employers, worried about losing top performers and attracting talented women in years to come, are beginning to help. They are offering alternative work patterns, from flexible hours to job sharing to telecommuting. In the process, they may be changing the nature of work for men and women.

Reshaping work to help a man raise a family is alien to corporate orthodoxy. To reach the top, many executives have sacrificed their "outside" lives. Managers, often wedded to bureaucratic ways of assigning work and evaluating it, resist new work styles. But adapt or die. Between now and the end of the century, women will make up 65% of new entrants into the work force. They bring more of the skills employers want. Among new graduates, women now account for 13% of all engineers, 39% of all lawyers, and 31% of all MBAs. The choice is either "flex" to accommodate women's needs or lose some of the best women who do.

The numbers are small, but employers are moving to protect their investment in



'The long hours were hard. I got up my nerve and went to see my boss'

KATIE GLOCKNER barely slowed her pace when her son, T.G., was born. But soon she felt she had to. "I was nursing the baby, and babies don't want to wait until the 6 p.m. meeting is over," she says. "I didn't feel

comfortable giving up so much of the care. You can fall in love with those little people." Glockner's boss at Quaker Oats, marketing director Polly Hallett, has no children but was supportive when Glockner suggested going on a part-time track. "She stuck out her neck and sold the idea," says Glockner, who now works three days a week as a brand manager.

top-flight women. In accounting, law, and consulting, part-time options and slower tracks to coveted partnerships are becoming established options. At some of the largest corporations, managers and professionals are experimenting with part-time work. Hundreds of companies let employees begin and end the workday earlier or later than the norm. Telecommuting—staying in touch via phone and modem—has taken off in Southern California, where just getting to work and back can use up three hours a day.

Many women believe they can slow down at work for a few years, get their kids launched, and come back with renewed zest. But even if more corporations accept that notion, the implications are not

to everyone's taste. Opponents see something insidious: a mommy track, separate and unequal, that will permanently derail women's careers, making them second-class citizens at work and confirming the prejudices of male executives.

The mommy tracker "puts up a sign: Don't consider me for promotions now," says Betty Lehan Harragan, author of *Games Mother Never Taught You*. Feminists believe that raising children should not be solely a woman's concern. The mommy track, they argue, means giving up the good fight—for social and family changes that would help mothers have full careers while fathers share more nurturing responsibilities.

Felice N. Schwartz has set the controversy boiling. In a recent *Harvard Business Review* article, Schwartz, the founder and president of Catalyst, an advisory group on women's leadership, set out what some see as a justification for second-class treatment of mothers. Employers, she argued, should identify and nurture two separate groups. Treat high-potential "career-primary" women, most of whom will be childless, just as if they were talented men. Then help "career-and-family" women be productive—but probably not upwardly mobile—by supporting their need for child care and flexible hours.

"The high-performing woman who does want to participate in the rearing of her children and is willing to trade off some career growth and remuneration for the freedom to do so will be happy at middle management for a significant period of her life," Schwartz says. She insists

that having talented, committed women at those levels—working and not competing—"will also serve to upgrade middle management."

The notion of two classes of corporate women, only one of which makes it to the top, doesn't sit well with Faith A. Wohl, a director of employee relations at Du Pont Co. "I'm not sure we should honor lack of family as a criterion and value women who are willing to put it aside," says Wohl. She argues that in this day of two-earner households, with more fathers taking responsibility for home and children, the nature of corporate careers has to change for everyone. Du Pont is trying to remold its culture along these lines, says Wohl. "Do we need as many relocations as we've



'I was bored and lonely. I thought that I would never work again.'

BONNIE MILLIMAN worked summers for Corning Glass, then joined the company as an engineer. Quitting after her first child was born was "big-time conflict." She took flak from friends who worked full-

time. Being in the house all day drove her wild. "My husband used to come home and scrape me off the walls," Milliman says. But being on call around the clock at Corning's hot glass plant didn't suit her life as a new mom, either.

Milliman began teaching engineering on and off at the local community college. Along the way she had another child. Eventually,

she worked with the college to set up a robotics center linked with Corning. That gave her valuable corporate contacts just when new part-time jobs were opening up. In 1987, Milliman took one—and she may have changed Corning in the process. "In retrospect, I made the tough decision that helped them see that there was a need for flexibility," Milliman says.

always thought, for example? Can a person have a period of part-time work—and still be considered for promotions?"

Equity, not mommy tracks, should be the goal, says Wohl. Critics also see favoritism: So far, most companies make such special arrangements only for a few, highly valued managers and professionals. Indeed, many companies refuse to publicize their policies for this reason.

There is no question that good child care, decent maternity leave, and partners

who pull their weight at home are essential for working mothers and wives. Social support for single parents is more critical still. But there are other issues: time, which is finite, and the emotional pull of parenthood, which is not. And a woman's expectations of what it means to be a good mother are highly individual and can't always be separated from her own upbringing. The result can be conflict.

Consider Katie Glockner, 31. A brand manager at Quaker Oats Co., she barely

missed a beat at work when her son Thaddeus G. Seymour Jr.—T. G. for short—was born in 1986. But by the following year, Glockner had had enough of long hours and week-ends. She asked to go part-time. "I loved my job. I was always career-oriented. But I had forgotten the fact that you fall in love with these little people, and I didn't feel comfortable giving up so much of the care," Glockner says.

MORE MATURE. Chicago-based Quaker had moved a few women from line to staff positions in the past, cutting their hours on the way, but a part-time brand manager? "I was the guinea pig," says Glockner. Quaker turned her request into a pilot program. She worked with higher-ups to set objectives. There were quarterly reviews. Personnel documented everything. Now, Glockner tends fewer brands and makes less money, but she has Mondays and Fridays free for T. G. Two other brand managers have followed her lead.

Role-conflict blues never bothered Margaret M. Hovell, a director in the personal systems line of business at IBM, in White Plains, N. Y. "I tell the children one of the things mommy likes to do is work. That has gone over very well," she says. Hovell joined IBM as a programmer right out of college in 1963. She followed a classic career path of trans-

fers and new assignments. She waited until age 38 to start a family, taking the standard maternity leave after each of her two kids was born. Away from home 10 hours a day, she manages well—thanks to a live-in nanny and a paragon of a husband who "also gives 100%."

But in 1986, there was one little problem. "My son needed his mother as he entered school," Hovell says. After 23 years with the company, she gave up her senior-level job as a divisional director of info-

ON THE MOMMY TRACK: W

ALTERNATIVE CAREER PATHS



Attorneys at Skadden Arps can work part-time, be associates or "special counsels." They work for a salary and may lower their odds of becoming partners. At Arthur Andersen, accountants who want to become partners in the firm receive credit for part-time work.

EXTENDED LEAVE



One of the most generous employers in this area is IBM, where employees can take up to three years off—with benefits and the guarantee of a comparable job on return. One requirement: Leave-takers must be on call for part-time work during two of the three years.

FLEXIBLE SCHEDULING



This often had ad hoc, but NCNB's office Employees customized schedules and work at home. Most who chose their hours worked thirds time and paid pro rata. mothers can "in" after six months maternity leave.

ation systems and took a leave of absence for 18 months. Such departures may soon be more common: IBM recently announced that it will offer all employees up to three years of personal leave with paid benefits and a job when they come back. The "quintessential fast track," says Howell, "has given way to a 'much more mature and balanced view.'"

In 1985, Christina Ling, 38, left the corporate world after she and her husband, a city planner, spent three years juggling careers. A former manager of financial planning and analysis at SmithKline Beckman Corp.'s Allergan Inc. division, Ling—who used to do grocery shopping on her lunch breaks—reflects: "I knew I couldn't keep working nights and weekends and being my child 45 minutes a day just to get the positions I wanted before."

CHANGING PRIORITIES. It's not that most women in management and professions are bailing out. Many view work as an integral part of their identities, just as men do. And most must work to maintain a certain standard of living. In fact, women with highly paid jobs and good benefits are more likely than others to return to work after giving birth.

Ling, however, now is running a home-based business—a well-trodden "outside" route for ambitious women. Still, it's second-best. "I want to return to a corporate job but without getting back into that rat race again," she says. "I think I could only make a three-quarter commitment."

As the new demographics force change, even the old prejudice against rehiring corporate dropouts is fading away. In 1982, Morning Glass Works lost Bonnie L. Milliman, a 26-year-old engineering supervisor. A new mother, Milliman balked at returning to 50-to-70 hour weeks overseeing 15 engineers, so she quit. "I knew I'd be splitting my priorities too often," she recalls.

Eventually, priorities changed at Corning. In 1986, a company survey revealed that women were not becoming top managers and that they were twice as likely to leave as men. Just replacing them cost more than \$2 million a year. Corning's isolated location in upstate New York was a



'I miss the challenge, but not the stress of being Superwoman'

CHRIS LING might have had it all, but she couldn't do it all. As a corporate financial planner she was her family's main breadwinner, as well as its day-to-day manager. "I have a very nice husband, and he lets me run the household," she says. Ling dropped out and started a business. Her company, Just an Idea, makes a plastic dishwasher basket for the tiny spoons and baby-bottle nipples that fall through a standard rack. She makes less money than she did in her former job, but she picks her own hours and needs child care only two days a week.

factor, but its maximum-devotion work ethic made things worse. "A new mother was really kind of stuck," says human resources head Thomas E. Blumer. Now Corning offers all salaried employees the option of working part-time or flexible hours. Twenty-five women signed on in the program's first year.

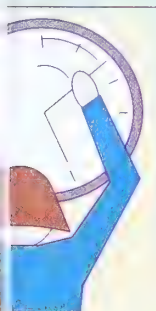
Milliman, now the mother of two girls, aged 7 and 4, was lured back to Corning in 1987. She is a project engineer, at the same level as the job she left, but she works only two days a week. Her husband, Bruce, is manager of office systems at Corning, and she is completing an executive MBA at Syracuse University, at compa-

ny expense. "When she left us, she was touted as a high-potential, senior-level manager," says Blumer. "Hopefully, she still can be."

Can she? That question is at the heart of the mommy-track debate. On one side, is Catalyst's Felice Schwartz, who argues that a few years on the slow boat shouldn't matter. Even if a female manager drops out for five years when her children are small, argues Schwartz, she would work 38 years as opposed to the typical man's 43 years—a barely perceptible difference. Indeed, a mother with school-aged children tends to be the most stable employee of all, says executive mo-

EMPLOYERS ARE HEADED

FLEXTIME



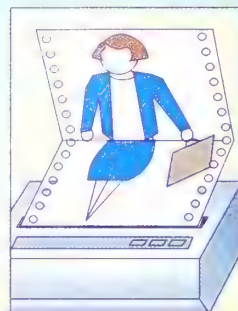
Less innovative than flexible scheduling, this is the most widely accepted Mommy Track reform. Any employee has the right to shift the standard workday forward or back by one hour. Thousands of public and private employers now allow such flexibility.

JOB SHARING



Not for everyone, but in some ways the most creative Mommy Track solution. At Steelcase, for example, two employees can share title, work load, salary, health benefits, and vacation. So far, the program is experimental and most participants are clerical.

TELECOMMUTING



The high-tech answer to being a working Mom. Some employers such as Pacific Telesis allow employees to limit the time they spend in the office by using personal computers, fax machines, and electronic mail at home. Perfect for many number-crunching jobs.



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'I wasn't penalized for part-time. There really are family values here.'

MIRIAM GOLD, a lawyer and mother of three, worked hard as a part-timer at Ciba-Geigy. "Lunches were short and breaks were few," she recalls—but the effort paid off. Gold, just promoted, has come back full-time as counsel to three divisions. She still reserves Fridays to work at home. That way, she says, she can "pick up my children from school and do things with them during the day."

busy expert Eugene Jennings at Michigan State University. "She's already gone through a lot of what causes women to leave," he explains.

Pacific Telesis Group, a company that has a tradition of lifetime employment—and a work force that's half female—takes the long view. "In the course of 32 years, an absence of two or three years is not the end of the world, and it's fairly common," says Jim R. M. Berg, vice president of human resources. "These people are going to be with us for a long time. I can't imagine being so rigid that you didn't understand that."

At Pacific Telesis, extended leaves of absence are more common than part-time jobs for managers. Still, after her first child was born in 1982 and her maternity leave was over, Linda E. Chinn arranged for eight months of part-time work. That helped her reorganize herself as a working mother for the long haul, she says.

'MARTYR SYNDROME.' For Chinn, now an assistant vice-president for finance, felt that continuing part-time work would compromise her future. She chose instead what she calls "the martyr syndrome," returning to 12-hour workdays, which she sometimes starts at 5 a.m. to have evenings at home. Chinn's husband, an emergency-room physician, works long hours, too. "My challenge is to

demonstrate that women can be women and be mothers and make it into the executive ranks," says Chinn.

And there's the rub. Baby-boom women who entered the work force 10 to 20 years ago are approaching their 40s—exactly when their male peers are making the big push into senior positions. Add to that the so-called glass ceiling—a cultural barrier many believe keeps women from the top. "First of all, a woman's going to have a harder time because the playing field's not level. The second issue is that she wants to take a few years off," says Mary Anne Devanna, who directs executive education at Columbia University's business school. "I think you'd be better off if you had your kids at 21, got them into school, and then went to work. If you want to be chairman of the board, your mid-30s are critical," Devanna maintains.

Only about 2% of corporate officers at major public companies are women. About 60% of top female executives do not have children, while 95% of the men do. The message seems clear: If you're a mother, don't

DADDY TRACK. Men who made it to the upper ranks have done so by relying on their wives to raise the kids and take full responsibility at home. A fast-track woman with an equally ambitious mate gets caught in a time and energy

crunch, even if both parents are equal partners at home. "I really think somebody has to cut back when the kids are small," says Gail Deegan, mother of five and seven-year-old sons, and chief financial officer of Eastern Gas & Fuel Associates in Weston, Mass. True, a full-time housekeeper gets dinner on her family table. But her husband, William R. Hurdleston, a clinical psychologist, also has reduced his sessions with clients to 20 a week at home. You might say he's on the daddy track.

Few men have been willing to buck cultural norms to that degree. And that leaves some critics to believe that men will simply leave the mommy trackers in the dust. "In most organizations, the mommy track is millstone around your neck," says Richard Belous, an economist at the National Planning Assn. In his recent study of 50 management and professional women who went part-time, Belous had to promise anonymity: Participants were nervous about just identifying themselves could hurt their careers. "CEOs and rainmakers don't come out of the mommy track," he warns. "If you go part-time, you're signaling your employer you're on the B-team."

Sometimes work places make that message explicit. At some elite law firms a Big Eight accounting firms, "permanent associate" jobs have been designed to halt the exodus of those who fail to make partner—and to accommodate women's needs. The new positions are more secure than the all-or-nothing gamble of traditional partnership tracks, and there's nothing to stop men from applying. But such jobs can relegate women to the least interesting cases and the fringes of power. Pa-

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ners, of course, also earn far more.

But Miriam V. Gold, 39, a division counsel at the U. S. headquarters of Ciba-Geigy Corp., insists she "really wasn't penalized" for her mommy-track years. An attorney and mother of three, Gold started at Ciba in 1977, cut her hours to three days a week in 1981, and recently returned full-time—for a promotion. As counsel to three large divisions and an operating unit, she works at home one day a week. Similar deals have been cut for only six Ciba managers—top performers whom the company didn't want to lose. "Miriam Gold is an exceptional lawyer," says Stanton Goldberg, Ciba's human resources director. Such arrangements, he believes, "should be restricted to high-quality employees."

Most companies also say that flexible schedules must be custom-tailored to work well. Some tasks can be done partly at home. Others may allow a shorter workday. Quite a few positions lend themselves to job sharing. At office-furniture maker Steelcase Inc., two women are sharing a dealer service representative job. They split salary, vacation, and benefits, working alternate weeks. Managers like the way job-sharing cuts down on absenteeism and helps fill the gaps during vacation time.

NEW YARDSTICKS. There is general agreement that jobs that can be done on a project basis are best suited to mommy tracks. Information-based jobs, where the files and the referencing system are stored in someone's head, are a lot tougher. And the consensus is that managing people cannot be done well at all. That's bad news for women, since corporations have traditionally measured career progress by how many bodies inhabit one's fiefdom.

This yardstick may now be outmoded, though. Downsizing has flattened many work organizations, with more people managing projects than supervising people. And even people managers often handle more than one department or delegate responsibility when they travel, which suggests that these functions can be segmented or shared. "What's the difference whether you're in Cleveland or at home with

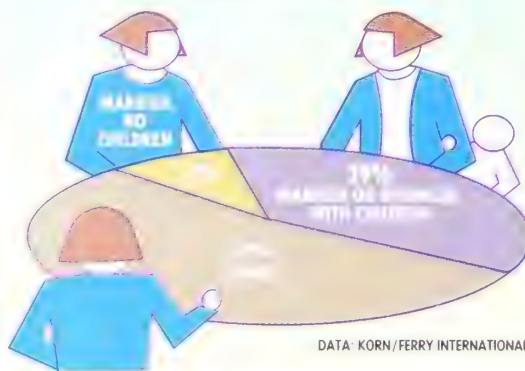
WOMEN ARE LANDING BETTER JOBS...

	Woman as percent of total	
	15 years ago	Now
MANAGERS & ADMINISTRATORS	20	40
GRADUATING ENGINEERS	1	13
GRADUATING LAWYERS	5	39
GRADUATING MBAs	4	31

DATA: NATIONAL PLANNING ASSN., BUREAU OF LABOR STATISTICS

...BUT FEW MOTHERS HAVE REACHED THE TOP

FEMALE EXECUTIVES



your family?" asks Corning's Blumer.

Moreover, an individual whose life is narrowly focused on work may not be the best manager of people, particularly in a time of growing work force diversity. Women's socialization, on the other hand, is precisely about getting along with other people. "When you're a mother or a father, you have to get everybody going in a constructive direction every morning. You have to have a sense of humor and keep your cool. Those things are very helpful in business life," says Ellen R. Gordon, who has four grown daughters and is president of \$114 million Tootsie Roll Corp.

Male-dominated institutions have never valued these skills. But as companies live with more women managers, they will have to examine the values they do hold. The question, really, is whether mommy trackers lose critical experiences and competence—or whether they simply break the organization's cherished rules.

Given the opportunity to experiment, managers

may come up with their own solutions. Last year, NCNB Corp., a bank holding company based in Charlotte, N. C., made an extraordinary offer to accommodate family needs with flexible schedules for each of its 14,000 employees. No men have applied. But Vice-President Patricia Goolsby, 39, who oversees corporate cash management services, jumped at the chance.

She reorganized her 11-person staff into independent teams so that they would not need constant access to their boss. Goolsby began leaving at noon on Thursdays and Fridays. That gave her time to get her daughters, ages 5 and 8, to Girl Scouts and dance classes, and to volunteer tutor the older girl's classmates in math. She must sometimes put in extra hours, but only after the kids are asleep. NCNB's program "is going to give us a clear recruiting edge," says career development director Karen Geiger. "Other companies are starting to do it, because they know we'll take their people."

The new work styles have their problems. Part-time professionals often find the hours stretching into full-time and are less likely to get "invaluable" sponsorship from higher-ups. Working at home is no panacea either: Even with a computer in your den, you still need a baby-sitter. It's hard to be all business when your child gets on the phone with a client and says anything from "the washing machine's overflowing" to "I have diarrhea," adds Claudia Wyatt, who takes calls at home two days a week as a Chicago consultant (no relation) at Wyatt Co.

Wyatt, a compensation and benefits consulting firm, recently offered a part-time path—with the option of returning to the fast track. One of the first to request a reduced schedule was a new father whose wife had just delivered twins.

That just might be what the future will look like. For there is another side to the demographics that are reshaping the world of work. The 1980s saw the ethic of long hours escalate in corporations and professions, partly because the baby-boom generation was competing for career advancement.

As the boomers age, more men as well as women may trade the next rung on the ladder for other rewards—more time, the ability to try something new, or a better quality of life. The challenge for companies is to provide flexibility and a rainbow of options so both men and women can raise their families as they see fit and still contribute.

By Elizabeth Ehrlich in New York, with bureau reports



Some women 'will be happy at middle management for a significant period'

FELICE N. SCHWARTZ
President, Catalyst

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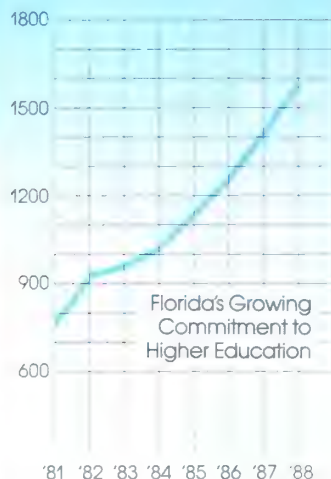
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Sports Business

STADIUMS

AFTER SKYDOME, STADIUMS WILL NEVER BE THE SAME

Toronto's revolution may even make money right off the bat

Baseball was never meant to be played indoors. Minnesota Twins and Seattle Mariners fans will be the first to tell you that. Their domed stadiums are the most depressing examples of the trade-off required for protection from bad weather. That's a big reason why Toronto spent an extra \$80 million to equip its new stadium with a roof that opens and closes mechanically. When the Toronto Blue Jays move into the 53,000-seat SkyDome on June 5, they'll have the option of playing indoors or out. But even more amazing than the engineering feat is the forecast by SkyDome owners that the \$360 million stadium will make money from the day it opens.

Profits and stadiums usually don't go together. Consider New Orleans' Superdome. Built 14 years ago for less than half the cost of SkyDome, it still requires a yearly state appropriation of more than \$6 million to cover operating losses. In contrast, SkyDome officials expect their stadium to generate \$20 million in cash flow in its first year.

What's going on? Nothing less than a revolution in the stadium business. SkyDome's financing scheme (table) is a model of how public spending can be minimized in building sports palaces. Even more important, by placing the stadium in the heart of downtown and designing it as a mixed-use entertainment center with a hotel, restaurants, and retail mall, Toronto is redefining the very concept of the stadium.

MAKING A STATEMENT. Toronto entered the big leagues in 1977, when it won an American League expansion franchise. But the Blue Jays' home was decidedly bush league. Most seats in drafty Exhibition Stadium, built for the Toronto Argonauts of the Canadian Football League, are in a left field grandstand that angles away from the diamond. As fans grumbled, Ontario Premier William Davis decided in 1982 that a new stadium must be built. But he didn't want a mere dome—even Vancouver had one of



SKYDOME AND ITS RETRACTABLE ROOF

WHERE THE MONEY CAME FROM

Millions of U.S. dollars	
BANK LOANS	\$120.8
VENDORS AND CORPORATE INVESTORS	117.6
PRESOLD BOXES AND SEATS	50.4
ONTARIO GOVERNMENT	25.2
METRO TORONTO GOVERNMENTS	25.2
PUBLIC STOCK SALE	16.6
ADVERTISING RIGHTS	4.2
TOTAL	360.0

DATA: STADIUM CORP. OF ONTARIO LTD.

those. Toronto had to make a statement put itself on the map. It had to have the world's first full-size stadium with working retractable roof. (Unlike the fabric version in Montreal that's kept closed because it tears when removed.

Davis turned to businessman John Trevor Eyton. The province of Ontario

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and the Metro Toronto council would kick in \$50.4 million if Eyton could get private investors to come up with \$40 million more. But as the scope of the project grew, it became clear that more private money was needed. Eyton ended up persuading 28 companies to put up \$4.2 million apiece. The roster includes heavyweights such as Ford Motor, Coca-Cola, Merrill Lynch, McDonald's, and units of Exxon and RJR Nabisco.

EXCLUSIVE DEALS. To woo investors, Eyton proposed an intriguing blend of philanthropy and profit potential. Each investor was promised use of a luxury skybox rent-free, parking spaces, and guaranteed advertising rights inside the SkyDome. More important, many locked up lucrative exclusive-supplier deals. McDonald's Restaurants of Canada Ltd. is building its largest restaurant in North America inside the stadium and will operate all concession stands. Coca-Cola Ltd. secured a 99-year exclusive soft drink contract. Merrill Lynch Canada Inc. will underwrite a stock offering.

A debate is still raging over whether Eyton gave too much to the corporate sponsors. But it's doubtful the stadium would have been built without a key concession by companies linked to Eyton.

The stadium corporation—not the team—gets to keep the \$20 million annual rental income from skyboxes. Eyton is president of Brascan Ltd., part of the Toronto Bronfman family empire. Brascan controls brewer John Labatt Ltd., which, in turn owns 45% of the Jays.

There's no need to shed tears for the team, however. SkyDome's season-ticket sales of 25,000 are up 66% from last

Each investor was promised a luxury skybox rent-free, parking spots, and advertising rights inside the stadium

year. A 1988 construction strike delayed the stadium's opening by two months, so the team probably won't break the Los Angeles Dodgers' 1982 attendance record of 3.6 million this year. But club officials think the Blue Jays may top that in 1990, when the team plays a full 81-game home schedule in the SkyDome.

In addition to income from the skyboxes, Stadium Corp. of Ontario Ltd.,

which owns SkyDome, will get a big chunk of the 37% cut from McDonald's concession revenues. And since the stadium is adjacent to the convention center downtown, it's expected to be used at least 200 days a year for sporting events, concerts, conventions, and trade shows. That explains the optimism concerning early profitability.

Although the mechanical SkyDome roof has passed preliminary tests, American cities are waiting to see if it works on a regular basis before copying it. There's less reticence in Japan. As many as 20 retractable-roof stadiums may be built there in the 1990s. The most dramatic is a \$1.6 billion project. Daiei Inc. Japan's largest retailer, says it will build a two-dome complex there: One will be stadium for its Daiei Hawks baseball team, the other, a shopping mall.

Back in Toronto there is one problem: a retractable roof will not solve: seagulls swooping in from nearby Lake Ontario. Management is balking so far at a contractor's bid of \$100,000 a year to provide falcons to keep the skies gull-free. But SkyDome may have little choice. Such are the costs of playing real baseball—out of doors.

By Chuck Hawkins in Toronto

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Foreign traders and methods are rocking Japan's stock markets

With the Tokyo Stock Exchange racking up a stunning 33% advance last year and an additional 6% already in 1989, foreign investors are flocking to Japan. Since Jan. 1, they have made net purchases of more than \$5.5 billion worth of Japanese stock, almost as much as the \$6.8 billion in all 1988 (chart). But Americans and others are doing more than pouring cash into stocks. They are trading vigorously, building up their staffs, and jolting the *Kabutocho* stock market district with high-voltage Wall Street strategies such as program trading.

Over the long haul, such activities by Salomon Brothers, Merrill Lynch, Morgan Stanley, and other Wall Street heavies threaten the very predictability that attracts them to the Japanese market. By introducing a new degree of price volatility, the foreigners now are putting in doubt Japan's long-held ability to muscle stocks upward—or protect them from disaster when times turn hard. "Cracks are forming," says Joseph G. Tompkins, managing director at Morgan Stanley International Ltd. "As this country internationalizes, Japan will lose some control over the market."

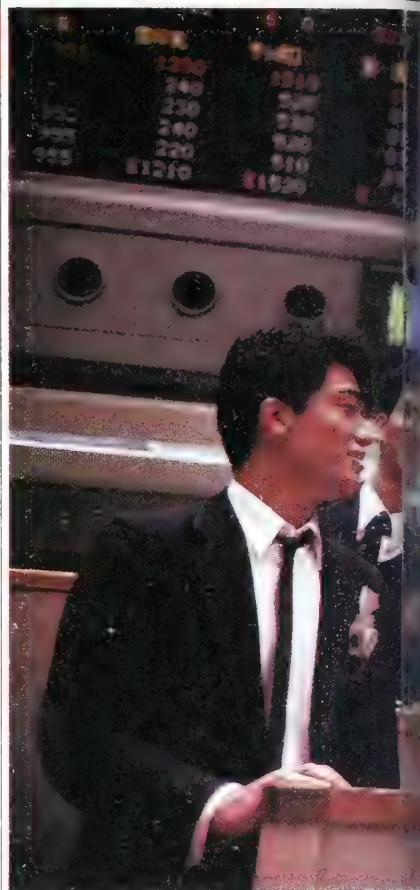
JAWBONING. Signs are already apparent that this is exactly what's happening. Foreign traders now account for an estimated 7% of Tokyo's daily volume, up from 4% only a few months back. In fact, the Ministry of Finance is so worried about losing its grip that it is imposing stiff new trading rules and jawboning Westerners to cool it. The actions were sparked by a surprisingly sharp 381-point jump in the widely watched Nikkei stock average last Dec. 7, the day futures contracts on the 225-share Nikkei and the Tokyo Stock Exchange's broader TOPIX index expired.

Under pressure from Washington and other allies, Japan has been opening its tightly controlled financial markets to foreign players for several years. One sign of progress, trading in stock-index

futures, got under way in Tokyo and Osaka last September. Business began uneventfully. But on Dec. 7, government and market officials were astonished to see a rush by U.S. brokers to buy millions of shares in the session's closing minutes. The buying wave sent the Nikkei average past 30,000 for the first time, embarrassing many Japanese brokers who had hoped to push the Nikkei over the top themselves a bit later—with enough time to alert local TV crews.

Like program traders back home, the U.S. buyers were taking advantage of a wide discrepancy between the prices of the expiring futures contracts and those for the stocks comprising the Nikkei (the Japanese Dow) and TOPIX (the Japanese S&P 500). "I was sitting at my screen, and you could see the Nikkei go up 50, 100, then 200 and 300 points," says Carmel Peters, director of Rothschild Asset Management (Japan) Ltd. "You knew the rise had been futures-oriented."

In response to the price jump, the Finance Ministry moved to head off a possible flood of stock sales as futures contracts expired on Mar. 7. It first barred brokers from trading in their own accounts during a session's last 30 minutes, when up to 40% of all index-related arbitrage trading occurs. Then, hoping to cut last-minute arbitrage opportunities even more, it ordered that futures settlement prices henceforth be pegged

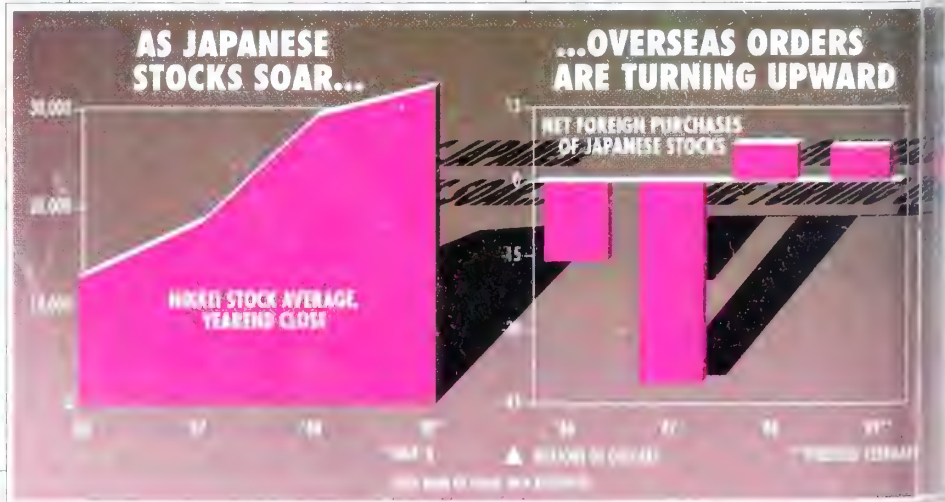


CULTURAL EXCHANGE: PROGRAM TRADING

to the next morning's opening quote instead of the expiration day's close.

The gambit worked: Futures contracts closed at a discount to stocks on Mar. 6. But traders neither dumped stocks nor rushed to buy the cheaper futures the next day. "The foreign houses were put off by all the attention," says analyst Keith Richmond at Jardine Fleming Securities Ltd.

But chances remain good that despite the Finance Ministry's moves, Western traders will mount even bolder challenges before long. Some New York brokers now are selling put options on the Nikkei average. Options on individual stocks, already available in the U.S.





UNDERMINE THE PREDICTABILITY THAT MADE TOKYO SO ATTRACTIVE IN THE FIRST PLACE

Japanese issues, will debut in June and two months later in And futures contracts based on the stocks are expected to begin in Chicago later this year. The big brokers likely will pile the futures game soon, too. The Ministry is expected to ease regulations that have shut them out of intraday, both by limiting their ability to trade stocks for their own account and preventing them from hedging their positions through selling stock prohibitions that do not apply to firms. Rothschild's Peters beholds that as a result of the swift move, "this market is going to be fun." But it may make it harder to trade the Tokyo market in the long run.

DOOR. Program trading isn't only foreign influence forcing its way on Japan's stock market. Nine banks now manage a token amount in private Japanese pension funds. By fall, Japan is likely to allow foreign brokerages and other money-management firms to go after private assets, too. Foreigners well-versed in futures, options, and other trading strategies may be able to convince Japanese investors that they can get better returns than the modest ones available from Japanese houses. Insider-trading scandals in the U.S.

also are changing the Tokyo market's way of life. Regulators are cracking down with a vengeance on insider trading and stock manipulation, which long have been regarded in Japan as innocuous ways of sealing business relationships. Over the past year, the Finance Ministry has pressed securities houses to keep hot tips on corporate-finance clients from leaking to brokers and salespeople. And on Apr. 1, a new law making insider trading a criminal offense will take effect. But in moving so aggressively, regulators are threatening to loosen many venerable ties between the market and the political and corporate elite.

Since last summer, the focus of the crack-down on insider trading has been the widening scandal at Recruit Co., a fast-growing conglomerate (page 55). Recruit's ex-chairman, Hirohisa Ezoe, is alleged to have made secret gifts of shares in a subsidiary to numerous executives and politicians, including many with

ties to Prime Minister Noboru Takeshita and his predecessor, Yasuhiro Nakasone. The affair is shaking Japan's faith in its stock market. But although insider trading is drawing the strongest scrutiny ever, shady dealings aren't passé.

'OLD TRADITION.' Tokyo's four largest brokerage houses, which control more than half of the nation's stock market activity, continue regularly to help politicians and other favored clients by running up selected issues for them. In an otherwise inexplicable move, for instance, Fujita Corp. shares already have doubled this year. On Mar. 7 alone, volume in the midsize construction company rocketed to nearly 100 million, 10 times its typical volume. Says one senior Tokyo banker: "The act of giving gifts is a very old tradition in Japan."

In fact, despite moves by regulators and foreign players to model Tokyo more along Western lines, many local traditions will live on for a long time. Few expect the Finance Ministry to abolish the fixed trading commissions that assure hefty profits for the big four brokers—Nomura, Daiwa, Nikko, and Yamaichi. And the government isn't likely to abandon ties to key brokerage and exchange executives that allow it to pick up gossip and communicate directives.

Nor is the government likely to cease its practice of steering Japan's abundant savings toward stocks. It has opened the way for as much as \$16 billion to flow into stocks this year by relaxing restrictions on equity purchases by several large public institutions. Factor in Japan's hefty 4% growth rate, and it's no wonder that Misao Meahara, a director at Nikko Securities Co., confidently pre-

dicts the Nikkei average will hit 37,000 by yearend—a 16% gain.

But the wider Japan opens its stock market's doors to foreign investors and their ideas, the more open the market will be to surprises. Says Morgan Stanley's Tompkins: "The Japanese believe that without foreign investment, this market would purr along like a well-oiled machine." Trouble is, with markets going global, a growing foreign presence seems unavoidable—as does a loss of the manageability that made Tokyo the envy of market mavens worldwide.

By Ted Holden in Tokyo



ROTHSCHILD'S PETERS: "THIS MARKET IS GOING TO BE FUN"

MONEYMEN MAY STOP DEEP-SIXING PROXIES

The Labor Dept. presses institutions to vote with care

It's proxy season. And if you own shares in a public corporation, the mailman will soon deliver a ballot and proxy statement. You might be asked to vote on housekeeping matters—electing directors or appointing auditors—or on bigger questions, such as a poison-pill antitakeover defense. But chances are you will not read the proxy statement—and won't even vote. In fact, only 50% to 60% of shareholders bother to cast ballots.

You might think, however, that the money managers who own stock on your behalf would be a lot more diligent in exercising their votes. If they didn't, they might well be shirking fiduciary responsibilities. It would be as though they lost a dividend check or squandered pension assets on penny stocks.

NO RESPONSIBILITY. You'd be wrong. Far too often, institutions are sloppy with their votes. Although many have upgraded their proxy efforts, a survey released by the Labor Dept. on Mar. 4 reports that 39% of the investment managers queried said they had no responsibility for voting the shares and didn't know who did.

The Labor report says that the following practices are among those that indicate a sloughing-off of fiduciary responsibilities by investment managers: failing to vote at all or not voting on controversial issues, blindly voting for corporate management's side without appropriate review, poor record-keeping, and an absence of formal policies outlining voting responsibilities.

The timing of the survey release was no more an accident than are Internal Revenue Service tax-fraud actions at income-tax time. It was "to provide guidance in advance of the proxy season," says David M. Walker, an Assistant Labor Secretary. Late last year there was speculation that Walker's office—which oversees corporate pension plans covered by the Employee Retirement Income Security Act of 1974 (ERISA)—was hunting for a "test case," a fiduciary that fumbled its votes. Walker now says that the enforcement-review effort is not

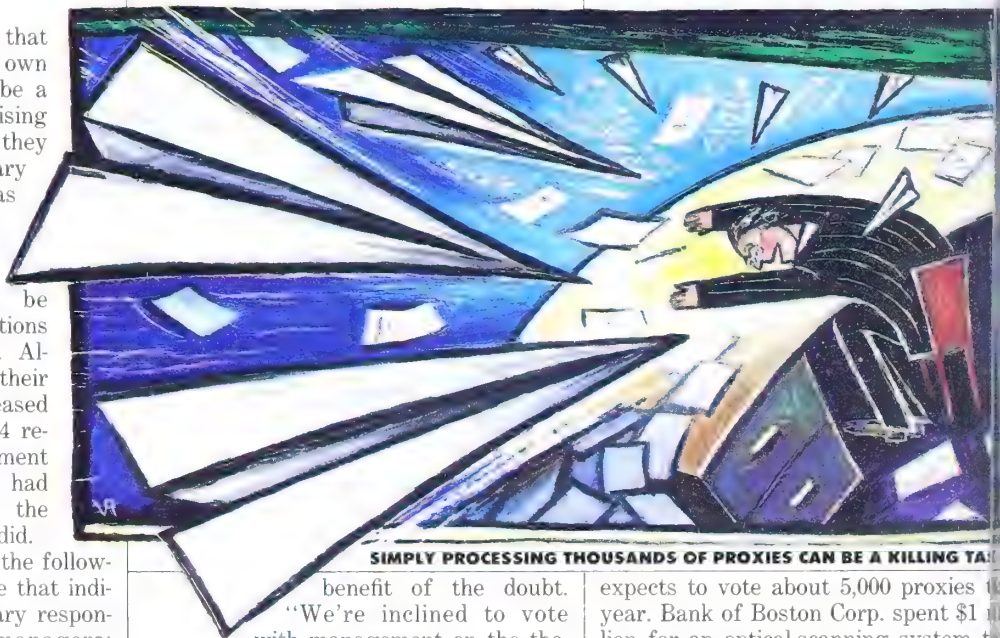
necessarily complete. Even without a test case, the Labor Dept. is making itself heard, says Robert Monks, president of Institutional Shareholder Services Inc., "and this will get people in line."

Historically, institutional investors have never put a big effort into proxies. They lived by the Wall Street rule: If you don't like management, you sell the stock. Even today, management gets the

an entire slate of nominees if the majority of them are from inside the company.

"We support management on issues that are routine," says William R. Hadeney, chief investment officer of First Union Corp. "Where we part is on issues that may impede or prevent a takeover of the company by outsiders." Indeed, most institutional investors surveyed by BUSINESS WEEK say their intake systems separate the routine from the red-flag issues—such as confidential balloting for shareholders or disengagement from South Africa.

WHEELBARROWS FULL. Just processing mundane ballot questions requires enormous efforts because of the sheer number of proxies. At United Asset Management Services in Denver, two or three wheelbarrows full of proxies arrive each day during March and April. At Wells Fargo Investment Advisors in San Francisco, Vice-President William McEwen



SIMPLY PROCESSING THOUSANDS OF PROXIES CAN BE A KILLING TASK

benefit of the doubt. "We're inclined to vote with management on the theory that if we like the stock we're generally approving of how management conducts affairs," says Peter R. Anderson, senior vice-president of Federated Investors Inc., a mutual fund manager.

In general, the institutions don't question management's choices of directors. "You don't go to each director and get an FBI report to see if he's drinking too much," says Robert A. McLaughlin, assistant director for investment at the Ohio Public Employees Retirement System. But at the giant California Public Employees Retirement System, one of the most active institutional investors in the area of shareholder rights, votes are cast against independent directors if they have any additional business relationship with the company. The California pension fund will also vote against

expects to vote about 5,000 proxies this year. Bank of Boston Corp. spent \$1 million for an optical-scanning system that will "read" proxies and enter them into its computers for record-keeping and analysis.

Some proxy officers at institutions welcome the Labor Dept.'s emphasis on fiduciary responsibility. They say it will help proxy voters resist pressure from corporate managers looking to sway their votes. A few pension-plan sponsors have decided that proxies are too important to be left to money managers. For the first time, a three-man team at Raytheon Co. will vote the proxies this year for the pension fund's \$1.4 billion in equities. With billion-dollar battles over corporate control being fought via proxies, shareholders' votes are an asset too valuable to waste.

By Jeffrey M. Laderman, with Tom Smart in Washington and bureau reporters

LIFE AFTER BOYD? AND HOW

Jefferies' Frank Baxter set a record in his first full year

The saga of Jefferies & Co. reads like the screenplay for a TV miniseries. The tale unfolds in 1962 when Boyd L. Jefferies implements the ideal idea of trading huge blocks of stocks 24 hours a day. After two decades of steady growth, his firm flies high in the 1980s when it executes big trades for high-rolling corporate raiders. Then the founder's worst nightmare comes true in March, 1987, when he resigns in disgrace to plead guilty to stock-trading-related charges. Shell-shocked employees worry that the firm may fold without him. But the new boss, Frank E. Baxter, emerges from his predecessor's shadow to restore order—and profits. Indeed, Baxter, 52, is on his way to writing a happy ending to the mess Boyd Jefferies left behind. In 1988, Baxter's first full year in charge, Jefferies & Co. earned a record \$16 million. The Los Angeles-based firm's earnings are higher than in every comparable quarter (chart). Baxter's steady hand was a major factor. "Everyone thought Boyd was the key," says Perrin Long, an analyst with Lipper Analytical Securities Corp. "But he wasn't. The firm is being managed more as a business, rather than as the whim of one individual."

OTHER FIGURE. At Jefferies & Co., Boyd Jefferies did it all. He took on the lobby Wall Street establishment and refused to join the New York Stock Exchange. He operated just a few freeways away from another finance maverick now accused by the government of illegal trading: Michael R. Milken, the Beverly Hills-based junk-bond wizard of Drexel Burnham Lambert Inc. Jefferies courted Ivan Boesky, Irwin Jacobs, and

he was a father figure to " says a former Jefferies trader. Now, stunning Executive Vice-President Alan D. Browning misses Jefferies by saying bluntly: "We're better without him."

Baxter is the reason. "I'm putting his stamp on the firm by boosting loyalizing costs, and steering it away from risk. To diversify revenues, Baxter

will start junk-bond trading and, perhaps, move into underwriting.

Baxter wasted no time showing he was in command. When he took over in March, 1987, his immediate goal was to build morale. So he promptly handed out 20% bonuses to all 180 of the firm's traders. He also reassured corporate and institutional investors that the firm would continue to execute major trades efficiently. But later that year, as business



CHAIRMAN BAXTER: "THE BEST FIRM IS A BORING FIRM. WE DON'T DO AS MANY MEGATRADES"

slackened, Baxter chopped costs 15%, largely by dismissing computer and support personnel.

Unlike Boyd Jefferies, who loved the big-but-risky trade, Baxter wants to broaden revenues and at the same time cut down on large gambles. Baxter ordered his troops to execute more, smaller trades. Now only 15% of the firm's trades involve blocks of more than 100,000 shares, down from 30% four years ago. Baxter has also cut the amount of the firm's capital used in trading to \$50 million, from a peak of \$300 million in 1985.

Last year the strategy paid off, amid the biggest year ever for takeovers. The firm made \$28 million

in pretax income, \$11 million of which came from risk arbitrage—investing in announced mergers and acquisitions.

The contrasts between the two leaders are striking. Former employees say Jefferies often handed traders \$1,000 in cash for 100,000-share trades. Jefferies also "would meet raiders behind a cactus on the golf course in Palm Springs," says Robert G. Kirby, chairman of Capital Guardian Trust Co. and a longtime client.

RECKLESS. Today, however, Baxter says: "The best firm is a boring firm. We don't do as many megatrades." Jefferies' flamboyance bordered on recklessness. When a trade of his cost the firm \$5 million in 1986—more than a quarter of its annual earnings, officials say—the indignant board made him pony up \$3.8 million.

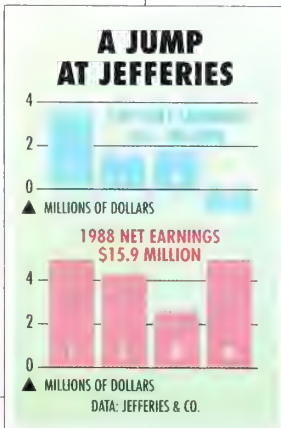
Worse yet was his gaffe of recruiting the business of British investor Alan

Clore. Jefferies & Co. began buying blocks of KaiserTech Ltd. stock for Clore in early 1987. After the crash, Clore couldn't pay the firm for nearly 1 million shares. Jefferies took a \$9.7 million pretax loss in the 1987 fourth quarter. Clore paid it all back in 1988.

Boyd Jefferies, who is awaiting sentencing on the federal charges, says: "I'm pleased the company is doing well." Small wonder—he still holds 13% of the firm's stock, in a trust. But Jefferies has no voting power over company affairs.

The founder's portrait still hangs in the firm's 33rd-floor lobby. And his settlement with the government permits him to come back in 1992. But with Baxter firmly in charge and business booming, there's no clamor for Boyd Jefferies' return.

By Eric Schine in Los Angeles, with Jon Friedman in New York



SUDDENLY, BLUE CHIPS ARE RED-HOT FOR ESOPs

A boon to morale and taxes, the plans can be poison pills, too

Long a refuge for small companies, the employee stock ownership plan (ESOP) is fast becoming a sanctuary for blue-chip giants. Procter & Gamble, General Mills, and Texaco are among those that recently added ESOPs to their menu of employee benefits—and to their arsenal of antitakeover defenses.

Most big companies, when they create ESOPs, stress the potential for enhanced morale and higher productivity. They're also clearly attracted by the tax-advantaged financing possible with ESOPs, which typically give shares to workers over a period of years.

While ESOPs date from the mid-1950s, takeover phobia in executive suites accounts for the current ESOP rage. An ESOP can be an awesome takeover barrier, since employees are more likely to vote their shares for the management they know than for the raider they fear.

Witness the classic takeover fight between Polaroid Corp. and Shamrock Holdings Inc., the acquisition company run by Roy E. Disney and Stanley P. Gold. A key maneuver by Polaroid in fending off Shamrock's bid was to set up an ESOP giving employees control of 14% of Polaroid's stock. Like many companies, Polaroid is incorporated in Delaware, where the law bars a hostile acquirer from merging with a target company for at least three years unless the bidder wins 85% of the stock. With its ESOP in place and after its current stock buyback, Polaroid would command enough shares to stall a merger.

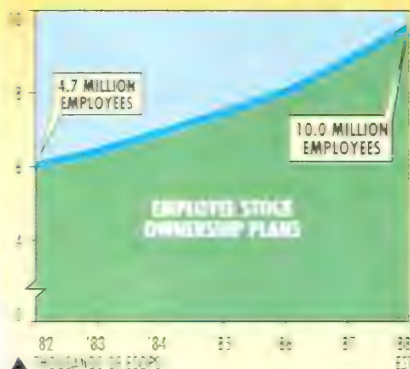
MOUTH-WATERING. No antitakeover defense is foolproof, however. Even though a Delaware court upheld Polaroid's ESOP defense on Jan. 6, Shamrock is appealing, and the law isn't settled enough to proclaim ESOPs the ultimate management weapon against corporate predators. And the Labor Dept. has warned Polaroid's ESOP trustee that the interests of management and employee-owners may not be the same: Trustees usually vote the ESOP shares not yet parceled out in the same proportion as those already held by employees, but in doing so they could be abdicating their fiduciary responsibility.

While merger mania is boosting corporate interest in ESOPs, other factors, too,

are entrenching the plans as a major corporate phenomenon (chart). Several studies have shown that companies that combine an ESOP with worker participation in decision-making enjoy sharply higher sales and earnings growth. And Congress, while tightening up elsewhere in its Tax Reform Act of 1986, actually made tax breaks for ESOPs even more mouth-watering.

A company borrowing to buy stock

ESOPs ARE SPREADING SWIFTLY...



for its ESOP gets to deduct not only the interest, as usual, but effectively its principal payments as well, on grounds that it is funding a qualified benefit such as a pension plan. The borrowed money is cheap, too. Lenders get taxed on only 50% of the income they receive on ESOP loans, so the rate they charge is typically 1½ percentage points below a company's normal borrowing cost. That's not all. The dividends a company pays on stock held by its ESOP are treated like interest—they're a deductible expense. And if at least 30% of a private business is sold to an ESOP, the sellers can avoid

Employees are more likely to vote their shares for the management they know than for a raider they fear

tax on the gain by using the proceeds to buy stocks or bonds of another American industrial company.

Understandably, the ESOP business no longer a cottage industry nurtured by a few visionaries. Top-drawer law firms, management consultants, commercial banks, insurance companies, and investment banks all extol the virtues of ESOPs to their corporate clients. Companies borrowed a record \$6.5 billion to fund ESOPs in 1988, and \$2.5 billion far this year. Says Robert E. Rice, partner in the law firm Milbank, Tweed, Hadley & McCloy: "An ESOP is becoming standard corporate finance."

GOOD CUSTOMERS. Companies are finding plenty of eager ESOP lenders these days. Profitable regional banks are buyers of ESOP loans; they're hungry for new tax-sheltered investments because tax reform rendered municipal bonds much less useful to them. Insurance

...EVEN TO SOME GIANTS

Company	ESOP's stake Millions of dollars	Number of employees
AVIS	\$1,700	12,500
HEALTHTRUST	1,700	23,000
PROCTER & GAMBLE	1,000	73,200
EPIC HEALTHCARE	886	10,000
J.C. PENNEY	700	177,000
PARSONS	560	10,000
TEXACO	500	54,000
WHITMAN	500	33,000
U.S. WEST	500	8,400

DATA: NATIONAL CENTER FOR EMPLOYEE OWNERSHIP

companies are active, too. Prudential Insurance Co.'s corporate finance group is working on a half-dozen or so private placement ESOP loans that could add to some \$650 million. The Pru already has \$1.1 billion out to ESOPs, including \$450 million to Procter & Gamble Co. and \$200 million to J.C. Penney Co. "These are high credit-quality companies that don't often come to the private placement market," says Prudential Managing Director Harry E. Knapp.

Congress has embellished the ESOP with lots of tax goodies out of a belief that for employees to own an equal stake in Corporate America is good for a free market society. And the ESOP movement is fast reaching the revolutionary stage: Employers are turning the means of production over to workers. Not under duress, but for tax breaks and safety from raiders. Ah, capitalism.

By Christopher Farrell in New York, with Tim Smart in Washington, Keith Hammonds in Boston, and bureau reports



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EDITED BY GENE G. MARCIAL

A BUYOUT GURU SHARES TWO TAKEOVER VISIONS

His name will never make the list of the big takeover players, but Leland Smith usually finds himself in the thick of corporate battles. Smith, president of Corporate Asset Strategies, is one of a handful of experts hired by companies under siege. And investor groups seeking to gobble up companies consult him, too.

Some of his recent clients include Texas financier Harold Simmons, whom he helped bag NL Industries; Xerox, which he advised on restructuring; and GenCorp, when it acquired RKO General. If a client is on the prowl, Smith evaluates a potential target's assets to discover hidden values. He also develops strategies for using hard assets in antitakeover schemes.

What companies does Smith consider ripe for takeover? He naturally won't discuss those he is studying for clients, but in his analyses of other companies, two very different candidates pop to the top of the list: Hewlett-Packard, a maker of computers, electronic calculators, and medical electronic equipment; and CalMat, a cement manufacturer.

Smith eyed Hewlett in November, when it was trading at 46. Now it's at 55. Despite the rise, Smith thinks the company is still attractive because of hidden assets. He believes Hewlett is worried about a raid even though its market capitalization is \$12 billion.

'IDEAL TARGET.' Estimates of the company's breakup value range from \$60 to \$70 a share. Hard assets, 75% of which are real estate properties, are worth \$6 billion, or \$30 a share, Smith figures. Since the company has very little debt, Smith thinks it will try to extract cash from the properties, most of which are in California, through sale-leaseback deals. It will then repurchase shares or possibly make a major acquisition. He notes that Hewlett has hired a real estate management firm to appraise and sell its properties.

CalMat has dropped from 34 to 27 in six months, but Smith says it's undervalued. The company values its properties, including real estate, at \$685 million, or \$22 a share. Smith pegs them at \$900 million, or \$30 a share. He sees a breakup value of \$55 a share.

"CalMat is an ideal target because it's property-rich and has the resources



SMITH: HEWLETT-PACKARD AND CALMAT ARE ASSET-RICH—AND VERY ATTRACTIVE

to fund a leveraged buyout," says Smith. The company has been selling assets to focus operations on its core cement business. Other operations include land development for industrial, commercial, and residential use.

Foreign buyers have acquired several domestic cement companies. And CalMat has one big Japanese shareholder, Onoda, with a 19% stake. If management doesn't take the company private, Onoda just might do it.

SCRAPPING OVER A FOOD PACKAGER

Interprise is about the best word to describe the goings-on between Envirodyne Industries, a major food packager, and Artra Group, a diversified company that owns 26% of Envirodyne. In mid-February the stock of Envirodyne shot up from 30 to 37, mainly on news of former Beatrice Cos. Chairman Donald Kelly's talks with management about a possible \$38-a-share bid.

Envirodyne may be the ultimate prize, but the first battle will be over Artra shares, say pros who have been snapping up Artra. Whispers are that British investor Philip Elghanian, who has raised his stake from 5.1% in November to 8.8%, plans to make a run.

One money manager says Elghanian wants to acquire Artra by teaming up with Artra President Peter Harvey, who owns 10%, either through an outright purchase or a leveraged buyout.

If they succeed, they'll control Envirodyne. But if Harvey resists, Elghanian will seek another partner. "Clearly the initial big fight will be over Artra," says one big Envirodyne investor who has started buying Artra shares.

Kelly could block Elghanian's plan by going after Artra himself. One shareholder puts Artra's value at \$60 a share vs. its current price of \$34.

WILL PETER GRACE CALL IT A DAY?

For over a year now, W. R. Grace has been a lackluster performer, locked in a trading range of 23 to 29. Yet some of the smartest institutions are high on the stock. Delaware Management owns just under 10%, and the Fidelity Group, including Peter Lynch's top-performing Magellan Fund, also has nearly 10%.

Part of the reason for Grace's allure may be its chairman's age. At 75, Peter Grace, who owns less than 1% of the company, might just give it all up and sell the company, which he has run for 44 years. Despite repeated claims that he won't retire soon, "Mr. Grace more and more, has been entertaining the idea from friends and advisers of making a dramatic move to get maximum value for the stock," says one investor. "And that means selling."

Mark Gulley, a specialty-chemical analyst at Dean Witter Reynolds, also thinks there are fresh signs that Grace will "do something with the company." For instance, Grace has sold some assets to raise cash for debt payment. And although many analysts disagree, Gulley thinks Grace might now respond favorably to an offer.

"Grace is an ideal LBO candidate given its excellent gross cash flow, steady and predictable growth, and the option of spinning off unrelated businesses and nonperforming assets," says Gulley. With a takeover premium, he says Grace's breakup value is \$75 a share.

Even if Peter Grace holds off, the conglomerate is still worth much more than the stock's current price would indicate, he says. Net of debt, here's his conservative estimate: Specialty chemicals, \$2.2 billion, or \$33 a share; specialty business, which includes plastic packaging materials, \$473 million, or \$5.60 a share; natural resources, including oil and gas exploration, \$64 million, or \$7.50 a share; health care, \$462 million, or \$5.50 a share; and others, \$406 million, or \$4.80 a share. Total: \$4.7 billion, or \$56.40 a share.

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Marrow and skin made outside the body improve on nature

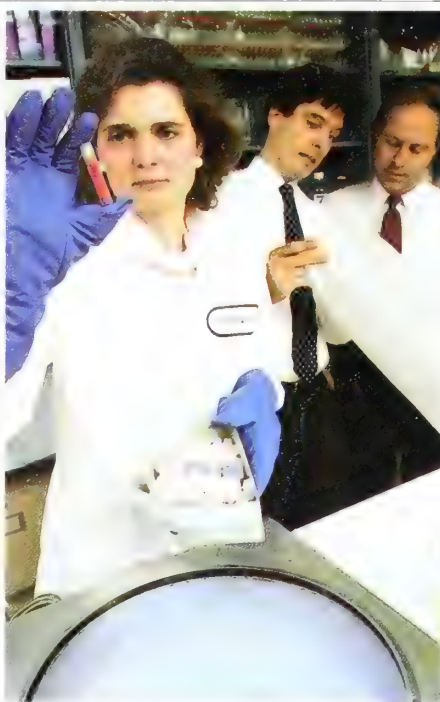
The small red vial in Gail Naughton's hand contains just a couple of teaspoonfuls of one of the most precious substances in the body: living bone marrow. Kill those cells, and the immune system is destroyed; red blood cells are no longer produced. Without frequent transfusions, death follows.

The destruction of those vital cells is just what happens in many cancer treatments. So before doctors prescribe heavy regimens of chemotherapy drugs or radiation, they increasingly extract the patient's bone marrow, store it during treatment, and then reinject it. The painful process requires a liter of marrow and about 200 needle punctures in the hip or pelvic bones during a three-day hospital stay.

Naughton, the founding scientist of Marrow-Tech Inc., thinks she has a better way: extract barely a tablespoonful of a patient's marrow—an amount that can be obtained in a doctor's office under local anesthetic—and culture it to produce enough for transplanting. The procedure is so easy that Marrow-Tech envisions healthy people at risk banking their marrow—those who work around radiation or highly toxic chemicals and those in high-risk cancer groups.

OFF-THE-SHELF. Culturing bone marrow in the laboratory is just one of the projects under way at the handful of biomedical companies that are growing human cells and tissues in the laboratory. Off-the-shelf skin and artificial blood vessels will also soon be ready for testing on humans. Scientists talk seriously of supplying patients at some later date with lab-grown livers and bones, growing contaminant-free blood, and correcting genetic diseases with lab-grown cells.

Even sooner, cultivated cells and tissues may create a lucrative market as alternatives for expensive—and controversial—tests on ani-



DR. NAUGHTON INSPECTS BONE MARROW

mals. With tests based on cultured tissues, "we are able to see how drugs work and how diseases happen and how to cure them," Naughton says.

Getting human tissue to grow in test tubes is no mean feat, however. While many kinds of cells will live in cultures, they soon stop multiplying in the absence of complex chemical signals from other cells in the body. So researchers

have had to mimic the environment of the body with growing systems where living support cells provide a surface onto which cultured cells cling.

With its culturing system, Marrow-Tech hopes to be the first company to grow bone marrow that will proliferate once transplanted into a human. The problem with cultured marrow in the past has been that it usually does not contain enough stem cells, the cells that continuously multiply to produce various types of blood cells. "The stem cells are a little like the Holy Grail," says Ron Cohen, medical director of the Elmsford (N. Y.) company.

Marrow-Tech says experiments with animals are encouraging: It has gotten test-tube marrow to grow in rats. Even so, concedes Naughton, "until we do actual transplants in humans we won't know the degree of stem cell activity we have." Those tests will begin next year.

REPLACEMENT SKIN. If the tests succeed, doctors will be able to attack cancer with heavier doses of chemotherapy drugs. Bone marrow transplants already have increased from 230 in 1979 to almost 2,500 in 1987. But the bone marrow can harbor cancerous cells. If a tablespoon-size sample is used to grow marrow, doctors have a better chance of weeding out cancer cells than they do purging them from a full liter.

Marrow-Tech and several other companies are also trying to develop replacement skin for the 22,000 burn patients who require grafts each year. The first skin substitute was developed by Howard Green, chairman of Harvard Medical School's department of cellular physiology, who devised a system for growing sheets of human keratinocytes, the outer epidermal cells, from small samples of burn victim's skin.

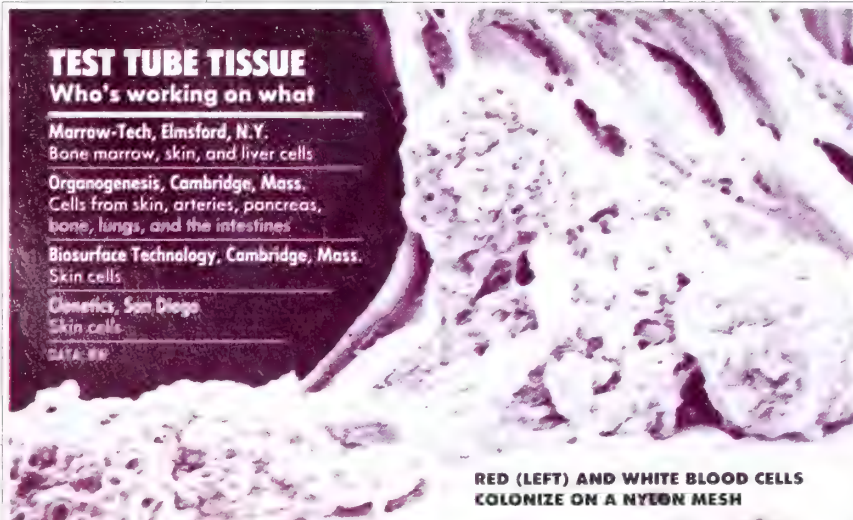
That process is now licensed to Cambridge-based Biosurface Technology Inc., which grows skin grafts and ships them to burn patients within a three-hour flight of Boston. "We can expand

postage-stamp-size biopsy one thousand fold in three weeks," declares Biosurface President David L. Castaldi. "That's enough to cover an entire body."

Others are trying to find ways to produce skin replacements that do not rely on the patient's own cells. These companies envision skin replacements stripped of the

TEST TUBE TISSUE Who's working on what

Marrow-Tech, Elmsford, N.Y.
Bone marrow, skin, and liver cells
Organogenesis, Cambridge, Mass.
Cells from skin, arteries, pancreas, bone, lungs, and the intestines
Biosurface Technology, Cambridge, Mass.
Skin cells
Clonetics, San Diego
Skin cells
DATA INC.



RED (LEFT) AND WHITE BLOOD CELLS COLONIZE ON A NYLON MESH

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ls that could trigger rejection, so it
uld be used without a three-week wait.
One of these, Organogenesis Inc., also
Cambridge, has developed a two-lay-
ed skin substitute that it calls a living
n equivalent. There is little indepen-
nt data to support the claim of the
npany's founder, Dr. Eugene Bell,
at the skin substitute is rejection-
proof. But Bell, a former researcher at
Massachusetts Institute of Technol-
y, believes he will be proven right
en tests on patients begin this year.
Marrow-Tech has another approach. It
ows its artificial base layer, or dermis,
eeding a biodegradable mesh with
roblasts, cells that produce the struc-
al protein collagen and other mole-
es that support cell growth. "Dermal
roblasts are usually not rejected,"
ys Naughton. Grafting this generic
rmis over a wound promotes healing
preventing the surrounding skin from
tracting, which leads to scarring and
id loss. After 10 days the surface of
e graft is sprinkled with the patient's
n cultured epidermal cells.

RAISING ANIMALS. In the short run, sup-
ring artificial skin and other cells for
icity testing will be the biomedical
npanies' bread and butter. In re-
onse to the animal rights movement,
oney is flooding into the development
test-tube alternatives to animal tests.
example, artificial skin can be used
test cosmetics and pharmaceuticals to
e if they produce irritation—instead of
ng Draize tests in which the com-
and is placed in a rabbit's eye. "Toxic-
testing is a business in itself," says
thur Benvenuto, Marrow-Tech's CEO,
who foresees a \$1 billion market.

Clonetics Corp. in San Diego hit the
rket first with Epipack, a kit that
as cultured keratinocytes to measure
emical toxicity. With requests for its
50 kit pouring in from laboratories,
netics is now branching into kits that
e pigment cells and connective tissue
ls. Meanwhile, Organogenesis recent-
received a patent on TestSkin, a kit
t uses its skin substitute. Marrow-
ch also plans to market a skin-test kit
yearend.

At the same time, the tissue-growers
e striving to meet more ambitious
als. Organogenesis is developing
od vessels with Eli Lilly & Co. It also
made an artificial rat thyroid gland
l is working on growing lung, intes-
e, and bone cells. Marrow-Tech hopes
technique eventually will help treat
netic diseases by culturing patients'
s, replacing any defective genes, and
n injecting healthy cells back into the
ly. Ultimately, the body's own tissues
y be the best medicine of all.

By Naomi Freundlich in New York



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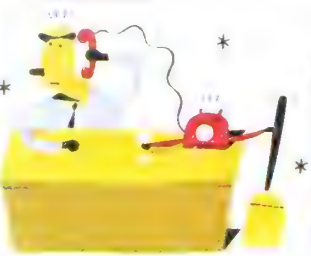


*From Database Magazine

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EDITED BY OTIS PORT

A PHONE NUMBER THAT FOLLOWS THE WANDERING EXECUTIVE



Where can I reach you?" To answer that question, Seattle executives no longer need to spout a string of phone numbers for their office, car, pager, answering service, and home. AccessPlus Communications Inc. in Bellevue, Wash., can provide them with electronic PALS—"personal access lines" that tag along wherever their users wander.

When subscribers change location, they just dial the PAL computer and tell it what to do by keying in codes on a Touch-Tone phone. Calls can be forwarded to any telephone or pager, much like current call-forwarding services.

In addition, AccessPlus has a sophisticated voice-mail capability that can screen calls at both ends. For urgent matters, the caller is told to press the zero key and dictate a short message. Then the computer puts the caller on hold, tracks down the subscriber, and plays back the message. The subscriber can take the call immediately or have it shunted to an operator or a recorder. Basic cost: \$26.50 a month.

AccessPlus plans to introduce the service in four more Western markets this year, then expand across the U.S. McCaw Cellular Communications Inc., a leading cellular telephone company, and former McCaw Vice-Chairman Edwin A. Hopper are among the investors in AccessPlus.

CHIPS: BREAKING RECORDS BY BILLIONTHS OF A SECOND

Speed records piled furiously on top of each other at the recent International Solid-State Circuits Conference. On one day a researcher from Hitachi Ltd. proclaimed the world's fastest high-density storage chip, a static random-access memory (SRAM) that needs only 9 billionths of a second (nanoseconds) to find one of the 1 million bits of data it can hold. SRAMs are similar to the familiar dynamic RAM, but their higher speed adds cost, so they are mainly used in expensive computers.

Hitachi's glory lasted less than a half hour—until the very next presentation. Then, Texas Instruments Inc. unveiled a 1-megabit SRAM with an access time of 8 nanoseconds. Even that record won't long endure, judging from other reports on experimental work with less dense SRAM circuits. For example, IBM has made a 128-kilobit (thousand-bit) chip with a 6.5-nanosecond access time. Hitachi also disclosed a 3.5-nanosecond chip. But swiftest of all was a Hitachi chip combining a 36K SRAM circuit with a so-called gate array. Accessing its memory takes a fleeting 2 nanoseconds. All told, Hitachi was tapped to deliver four of the eight papers on SRAMs.

HYDROGEN MAY HELP EUROPE KICK ITS FOSSIL FUEL HABIT

How much does a gallon of gasoline really cost? The price on the pump is just for starters. Tack on the hidden costs of related pollution, and the price skyrockets. That realization is spurring the European Community to take a fresh look at hydrogen as a lower-cost alternative, even though hydrogen costs four times as much, ergo for ergo, as hydrocarbon fuels.

The first put-up-or-shut-up evidence comes in the agreement just signed by the EC and Quebec province. They will conduct a joint five-year study, directed by Canada's Hydro-Quebec and West Germany's Ludwig Bolkow Foundation, on shipping hydrogen from Canada to Europe. If the initial paperwork evaluation looks promising, the plan calls for a multimillion-dollar hydrogen plant on the Saint Lawrence Seaway that would use Quebec's abundant hydroelectric power to split hydrogen from water (BW—Nov. 28), plus a ship that would carry 20,000 tons of hydrogen to Europe. The gas would be used as fuel for public transportation—both Hamburg and Milan are interested in converting their buses to the gas. Other uses: district heating in cities, to make electricity in fuel cells, and research.

GOING ANOTHER MILE TOWARD TURBOCHARGED CAR ASSEMBLY

Car companies shop for lots of parts on the outside, but they like to put them together in their own plants. Detroit has spent years debating a different concept, dubbed modular assembly, that would shift more of the assembly work to suppliers. But it seems that Europe may steal that march.

Starting in June, Rockwell International Corp. will ship its first door modules to a European carmaker, believed to be Fiat. The units include everything between a door's inner and outer panels: the door latch, window glass, and mechanisms to raise and lower the window. Because the modules slip together easily, the auto maker will save on factory space as well as labor and parts-tracking costs. Rockwell contends that even greater economies will come from improved quality, since each unit is tested before it reaches the assembly line.

Moreover, the new doors are a snap to repair. If something goes wrong, mechanics just do what TV repairmen do: Pop out the problem component and stick in a new one. It takes only minutes. For a comparison, Rockwell asked a mechanic to fix a typical window assembly. "Five hours later, he was still working on it," says William F. Rebore, president of Rockwell Light Vehicles Components Business.

THE FIN IS BACK —THIS TIME, ON TRUCKS

Tailfins on cars breezed out decades ago, but they seem poised to barrel back on 8-wheelers. The trucking industry figures that aerodynamically designed fins, by streamlining boxy tractor-trailer rigs, could save countless gallons of gasoline each year.

Developed by Continuum Dynamics Inc. in Princeton, N.J., the rectangular fins extend two or three feet from the back of the trailer. They channel some of the air flowing past the side inward, toward the truck's back end. This reduces the drag from the low-pressure pocket of air trailing the trailer. In fact, the air pressure can become higher than normal, giving the truck a forward boost. The fins fold back against the side when the driver pulls into a loading dock.

In wind-tunnel tests by NASA engineers, the fins cut drag on a tractor-trailer by 10%. The engineers thus calculated that the getup could pay for itself from fuel savings in one year. J. Bilanin, a CDI scientist, expects trailer manufacturers to begin offering the fins as original equipment within a year.



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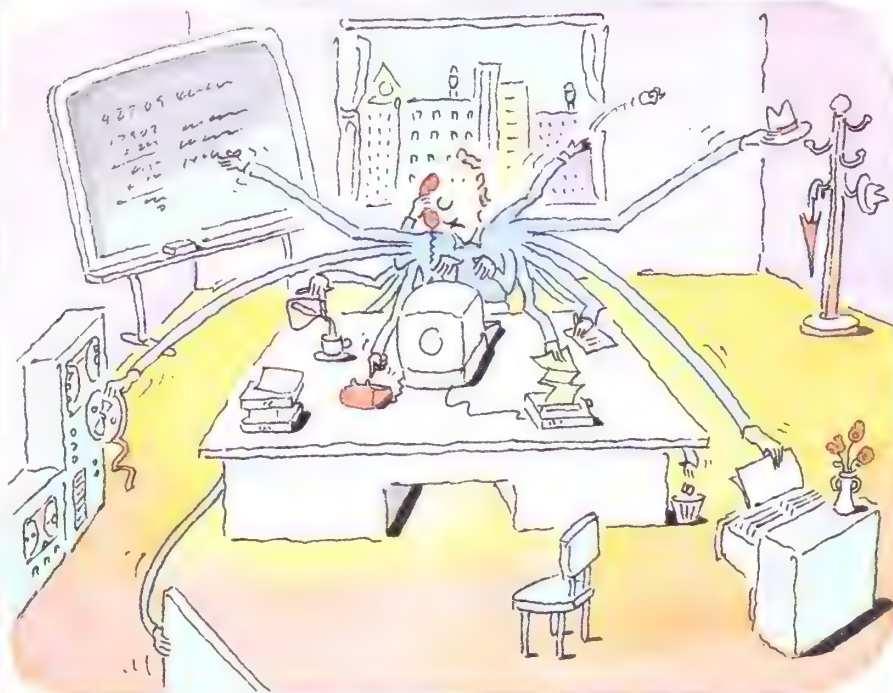
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IBM'S MICRO CHANNEL GETS A LITTLE RESPECT

The Rodney Dangerfield of computers builds a following

For years engineers at Northern Telecom Ltd. designed circuit boards the old-fashioned way: Each worked at a terminal hooked to a mainframe. The complex circuit-layout programs they used often slowed the system to a crawl. It took minutes for changes to appear on the screens, while highly paid engineers sat idle.

That changed last fall when the phone equipment maker got rid of the mainframe and put IBM Personal System/2 computers on each engineer's desk. To each PS/2 it attached a special IBM co-processor—an additional microcomputer that has the power of a small mainframe. The old mainframe programs, now able to run on each PC, work six times as fast, and productivity has increased 15% to 20%, says Ralph B. Alspaugh, a manager of technical services.

FULL SPEED. What makes Northern Telecom's system tick is a PS/2 innovation called the micro channel. It controls the flow of data between the computer's central processor and various components such as disk drives and communications lines. Unlike IBM's original PCs,

PS/2s with the micro channel can operate more than one processor at the same time. That way, the central processor can do its normal work at full speed while specialized co-processors attached to the micro channel perform hard tasks, such as displaying a detailed graphic image on the screen. Conventional PCs bog down when they run a complex program or several jobs at once.

Ever since it arrived two years ago, the micro channel has been the Rodney Dangerfield of innovation, fodder for jokes by competitors and customers who claimed that it sounded neat but had little practical use. IBM has yet to persuade a broad base of customers to switch to these machines, since they aren't compatible with older PCs, and little software for multiprocessing jobs exists. Nonetheless, the micro channel may at last be getting some respect.

New printed-circuit

cards that take advantage of the design are beginning to appear. Pacific Image Communications in Pasadena, Calif., sells a \$995 SuperFax MC card that lets a PC send and receive facsimile messages without interrupting other tasks. A San Diego-based Lantana Technology Inc. makes a \$795 card that lets a PC swap data across a local-area network "in background" while continuing to work on the screen. IBM claims that by year-end there will be more than 100 cards that use basic multiprocessing capability. And that promise is helping to build a modest but influential following.

Take Daryl C. Jackson, manager of office technology at PepsiCo Inc.'s research center in Valhalla, N.Y. Jackson recently set up a desktop computer network that connects 273 PCs to one micro channel PS/2 Model 80. The PS/2 coordinates the entire system. While some employees on the network record shipments of Pepsi-Cola concentrate bottlers, 32 others can send and receive fax transmissions or electronic mail. According to Jackson, with conventional PCs the flow of data often bogged down.

CONFUSION. IBM needs many more sales testimonials. Its share of the PC market already falling when it introduced the PS/2 and began promoting micro channel as its chief virtue, has continued to drop, from 37% in 1987 to 32.6% this year, according to StoreBoard Inc., a market researcher. This year, says International Data Corp., just 12.5% of all PCs sold by U.S. manufacturers will be micro channel machines, though that's almost 2 points from a year ago.

The snail's-pace growth partly reflects customer confusion. But IBM also made some mistakes, says Leslie Fiering, who belongs to the 600-member Micro Channel Computer Managers' Assn., a group of corporate PC buyers. IBM ignored what the original PC taught about so-called open architectures, says Fiering. IBM made it hard for circuit-board makers to get specifications to create add-on products and "next to impossible" for other computer makers to develop micro channel machines. Although clones are now appearing, micro channel has been essentially an IBM-only product.

That, along with slow customer acceptance of the micro channel, prompts competitors to propose alternative hardware designs. Led by Compaq Computer Corp., a group of PC makers dubbed the Gang of Nine announced last September plans to create an EISA, or extended in-

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try standard architecture, a multiprocessing design that is compatible with older IBM PCs. EISA, however, is not compatible with micro channel. That, asserts Richard J. Gough, IBM manager of PS product marketing, confuses customers. But EISA supporters counter that it created the confusion in the first place. It made micro channel proprietary and built PCs that were "completely, totally different," says Robert D. Kutnick, director of strategic projects at AST Research Inc., an EISA member.

ROLLING CLONES. Both camps are hedging their bets. On the very day that EISA was announced, IBM brought out a new micro channel PC, similar to the old IBM PC/AT design that clonemakers had continued to sell successfully—at IBM's expense. Big Blue is expected to add another AT-compatible machine using Intel Corp.'s 80386 chip this year. On the E

IBM is pushing micro channel with special dealer discounts, a public relations blitz, and prime-time TV commercials.

side, Tandy Corp. and Olivetti have advanced Logic Research Inc., a small rival, will begin shipping micro channel machines on March 17, and Dell Computer Corp. has a "clone" in the wings.

Meanwhile, IBM is pushing harder to win converts. It is offering special discounts to large dealers, has hosted numerous briefings for analysts and the press, and is plugging micro channel on prime-time TV. All that may be paying off. Computer Intelligence, a market researcher in La Jolla, Calif., estimates that 45% of all PCs purchased by 500 major U.S. companies this year will be micro channel models. For the moment, moreover, time is on IBM's side. The first EISA machines won't appear until next year. By then, almost 4 million micro channel machines should be in use.

That number is less impressive than it looks. Many customers say they bought micro channel only because it came with their IBM machines. And many PC buyers may never need the multiprocessing power of EISA or micro channel. So many others, such as David W. Hasiba, who buys desktop computers for Merrill Lynch & Co., think that micro channel is a good investment: IBM has promised to make it the centerpiece of the next generation of PCs. Adds Hasiba: "We're betting ourselves up for the future."

By Susan M. Gelfond in New York



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WHY BUSINESS IS GLUED TO THE TUBE

Companies find a handy new tool: Their own TV networks

Federal Express couriers start the day watching an internal TV report on route conditions. Texas Instruments uses a *Wheel of Fortune* knock-off to introduce products. With its satellite TV system, Domino's Pizza teaches employees to slice vegetables and make dough—the kind you bake, that is.

Whether as a tool for marketing, training, or public relations, business TV is booming. Last year there were 61 satellite-based business TV networks, up from four in 1983. Now Electronic Data Systems and GTE Spacenet, among others, are scrambling to enter the \$150 million market for satellite TV equipment and transmission services against such giants as American Telephone & Telegraph Co. Last November, EDS bought VideoStar Connections, a pioneer in business TV. Customers suddenly want more than just data networking services, says EDS Executive Vice-President Richard W. Pryor. "If we can't offer business-TV expertise, we'll be out in the cold."

HAM HEAVEN. The technology to build a private TV network has existed for nearly 10 years. But the equipment was expensive—more than \$5 million a network, including a studio, transmission center, and 50 antenna sites for receiving signals. And executives were camera-shy. Now they all want to be Lee Iacocca. And, says market analyst Susan Irwin of Irwin Communications, the price of a network has dropped 60%, to about \$2 million, as dish antennas get smaller and cheaper. That means the investment can pay for itself fast.

J.C. Penney Co. figures that reduced training and travel let it recoup the \$4 million startup cost of its 700-site network in one year. First Union National Bank in Charlotte, N.C., says its satellite data and video network will generate savings of \$3 million over five years, vs. using land-based phone lines. Two years ago, when the photosensitive drum in an Eastman Kodak Co. copier malfunctioned, Kodak had to replace the \$700 unit. But then it developed a \$50 fix for the congenital problem and rushed it to

71 field offices via TV, saving an estimated \$350,000.

Beyond that, there are endless PR possibilities. In early 1988 a Manhattan acting troupe, Plays for Living, persuaded J.C. Penney to deliver antidrug programming over its network. Last fall the retailer broadcast a drama featuring the troupe plus a discussion on teen drug

a deal with Citicorp via the banking giant's network. "We managed to get the people needed to make a decision in one place at the same time," says Hewlett-Packard's TV manager, Merle Ruomet.

FLAIR NEEDED. This interactive ability makes TV a powerful training tool. Domino's broadcast from Palm Springs, Calif., last year showed franchisees how its most successful outlet organizes its shop. ComputerLand Corp. trains repairers at 106 sites over its network instead of sending them to class. Service businesses, which account for 57% of growth, can thus better cope with labor shortages and lagging productivity.

Companies that can't afford networks can hire independent broadcasters. The Automotive Satellite Network (ASTN), the largest, reaping \$19 million a year



DOMINO'S PIZZA: IT USES TELEVISION TO TEACH FRANCHISEES HOW TO RUN THEIR SHOPS

use to 2,200 community groups gathered at 700 stores. That was "good for business," says Jeanette Siegel, Penney's community relations manager. "It shows people we care."

Another example: Last March, Texas Instruments Inc. linked its executives with reporters in five U.S. cities and Paris to discuss its efforts to integrate TI's Lisp artificial intelligence processor into Apple personal computers.

Now, TV is being used more for routine business as well. One of the largest networks belongs to Merrill Lynch & Co.

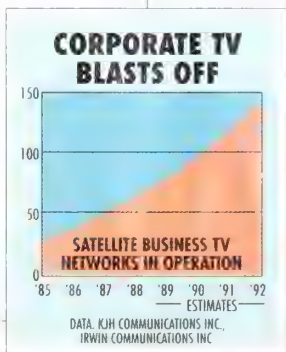
In 1984, Merrill found that mutual funds unveiled over its 450-site network sold 30% to 40% better than those that are sold through brochures. Customers tended to throw away the printed material but watched the TV show. Merrill also cut its sales overhead. Hewlett-Packard Co. officers recently closed

revenues from 3,000 dealerships. In June, ASTN plans to launch the Law Enforcement Satellite Network to train police officers. And other broadcasters are beginning to serve the food-processing, hospital, and securities industries. Industry observers expect that by 1992 there will be 141 TV networks, a 131% increase. TI may even give Emmy-like awards to its own best shows.

Not a bad idea, since the one major hurdle still facing business TV is program quality. HP's Ruomet says that many shows are just plain dull. "How many times can you watch a lecture about some car without going crazy?" asks one auto dealer.

He might take heart from a recent radical departure by ComputerLand. To keep its service people awake during a show, the retailer had employees of Novell Corp. introduce their software product with rap music. The rappers went over so well that Novell wants them to do live shows at industry conventions.

By Kevin Kelly in Dallas





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ADVERTISING

THE COLA SUPERPOWERS' OUTRAGEOUS NEW ARSENALS

A sneak attack by Coke escalates the hostilities

Oh, sure, Iran and Iraq have declared a cease-fire. And the last Soviet tanks have rumbled out of Afghanistan. But don't think the world is at peace. The AWACS are aloft over Atlanta, and they're breaking out the stinger missiles in Westchester County. That's right: The cola wars have erupted again.

This time, it was Coca-Cola Co. that launched a sneak attack on archrival PepsiCo Inc. in Purchase, N. Y. In a 3D ad splash that aired during the Super Bowl, Coke said Pepsi drinkers are switching to diet Coke. Pepsi fired back with an ad mocking the 3D glasses viewers had to wear to watch the ad, and poking fun at Coke's market research and its executives. Then each side complained to the networks about the other.

Coke had good reason to feel bellicose. Helped by its grip on the soda-fountain business, the No. 1 pop maker grabbed a stunning 40.5% of the \$27 billion U.S. soft-drink market last year, far outdistancing Pepsi's 30.7% share. But in retail stores, where consumers have a true choice and marketers look for real bragging rights, Pepsi gained steam while Coke, surprisingly, lost share in 1988.

That was largely because Pepsi has dominated the ad battleground lately

with glitzy ads featuring well-known stars such as Michael Jackson. Says PaineWebber Inc. analyst Emanuel S. Goldman: "Pepsi is outreating Coke." But Pepsi may wish that it had been a little less creative. On Mar. 2, it launched a big new campaign featuring pop singer Madonna with a \$5 million media extravaganza. Pepsi kicked off the ad, which featured the premiere of Madonna's new song, *Like a Prayer*, by buying two minutes of prime-time TV in the U.S. and 40 other countries. But days later, Madonna's music video of the same song created a furor because of its mingling of suggestive scenes and Christian imagery. Already, Pepsi has pulled its commercial from MTV, which is running the video, and the spot's fate elsewhere is in jeopardy.

While Coke hasn't suffered from such embarrassments, critics say its ad message has been perplexing ever since the 1985 introduction of new Coke. After a deluge of complaints from consumers and bottlers, Coke brought its original formula back as Coke Clas-

sic. But with two Cokes, the company's popular "Coke is it" campaign became meaningless, and the company dropped it in favor of the more ethereal "Coke beat the feeling." Says David K. Debra, whose New York-based Visual Storyboard Tests Inc. measures consumers' responses to TV ads: "Coke is really diffused."

BRAND EROSION. Worse yet, some current and former Coke insiders fear marketing took a backseat to discounting, a trend that could threaten the brand's image. Goldman figures Coke's U.S. ad expenditures dropped from \$159 million in 1985 to \$140.7 million in 1987, while Pepsi hiked its budget from \$116.7 million to \$135.8 million. "There was a lot of talk among many people that pricing promotion was the only name of the game," says independent bottler Henry A. Schimberg, who runs Chattanooga-based Johnston Coca-Cola Bottling Group Inc.

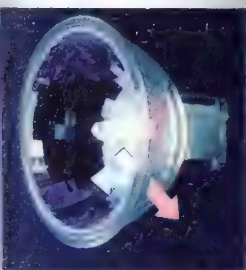
Some bottlers also worried about Coke's corporate distractions. Last year it spun off much of its troubled Columbia Pictures unit. And to take more control of its bottling operation, Coke created its Coca-Cola Enterprises Inc. subsidiary. The centralization of bottling forced a reorganization of Coca-Cola USA last year and a morale-damaging layoff of 200 workers. "We got lost inside ourselves," says Ira C. Herbert, who was named president of the domestic soft-drink unit four months ago. "Now we are looking to add some excitement and go on the offensive to reestablish our legitimate

A NARROWING LEAD



Shedding light on a natural phenomenon.

Leaves can separate light from heat. They reflect some of the heat, while the rest passes through them. They use only "cold" light in photosynthesis.



Schott's special glass reflectors also separate light from heat, allowing 95% of the heat generated by a light bulb to pass through the back of the reflector. The special silver dioxide coating which the lamp manufacturer puts on the glass reflects just the "cold" light, creating pleasant and natural lighting.

Concentrated light generates a great deal of heat. And because leaves are constantly exposed to strong rays of sunlight, they have a very special ability. To keep from drying out, they reflect a certain amount of the heat and allow the rest to pass through them. In photosynthesis, they use only "cold" light.

Reflectors in low voltage halogen lamps also separate light from heat, but in this case the process works in reverse. With the addition of a silver dioxide coating, they reflect "cold" light and allow heat to pass through the wall of the reflector.

_____ This can only be achieved by using glass, because unlike metal, it allows heat waves to pass through it. But of course, this application requires a special kind of glass. It has to be highly heat resistant and able to withstand thermal shock – especially when used in halogen lamps where temperatures exceed 4532 °F.

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Settled the American West

Union Pacific settled the American West, carrying hundreds of thousands of pioneers into the world of wide open spaces. It made history then, and it's *still* making history: today it is one of America's most progressive railroads, with 23,000 miles of track in 20 states, 30,000 employees, and a reputation for far-sighted thinking in every area of its operations—including its remarkable communications network.

Nationwide network

Union Pacific owns a private voice and data communications network, one of the largest in the world. Covering tens of thousands of miles nationwide and functioning as the railroad's central nervous system, it is extremely sophisticated and absolutely crucial to the company's success. Which is

why, when Union Pacific recently decided to upgrade the network, it turned to Fujitsu.

Number one computer maker

Fujitsu is Japan's number one computer maker, and one of the world's top telecommunications makers, with 100,000 employees, annual sales of \$16 billion, and projects completed in a hundred countries. A high-tech giant that's a major force in the global information revolution, Fujitsu gave Union Pacific a multi-nodal integrated voice and data communications system that is the next generation of business telecommunications. The system will boost productivity, upgrade customer service, and help the railroad keep making history—by helping it be what it has always been: a living legend that knows where the future is.



Jim Merrick of Union Pacific talks to Jay Schrimpl of Fujitsu before the Fujitsu F9600 ISDN switching system. Union Pacific recently purchased a number of such systems, the most advanced in the world, to function as node points in its nationwide communications network. For information call Fujitsu Business Communication Systems at 1-800-654-0715.



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1992 AND BEYOND

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Marketing

place in the behavior and minds of the consumer."

To do that, Herbert is trying an audacious and unusual strategy. Coke's new ads contend that regular Pepsi drinkers are switching to diet Coke. That, says industry analyst Jesse Meyers, marks the first time a company has pitted one of the faster-growing diet brands, which grew 8.4% last year, directly against sugared colas, which increased 4.4%. "This is an elegant marketing maneuver," Meyers says. Admits a Pepsi spokesman: "It hit home."

Why? Coke has already tried to get regular Pepsi drinkers to switch to regular Coke: Its new Coke was formulated to mimic Pepsi's sweeter, less-bitter taste. Still, the brand has so far managed to pick up only 1.4% of the market. But consumers are increasingly switching to diet soft drinks, and diet Coke



PEPSI'S MADONNA AD: CONTROVERSIAL

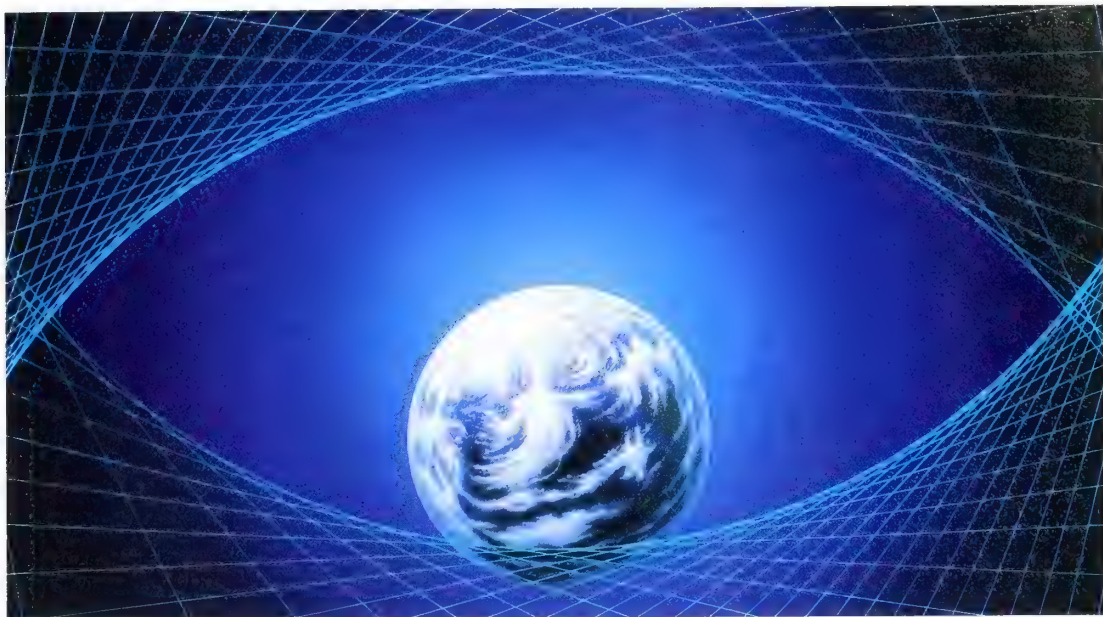
growing a bit faster than Diet Pepsi. Why not attack Pepsi with diet Coke as its point of strength? "An old military professor once told me to pick the battle field. Well, we're going to pick the battlefield now," says Herbert.

Coke has an advantage in the market. For years diet soft drinks were marketed chiefly to figure-conscious women. But with better-tasting NutraSweet formulations, a growing number of men are switching to diet colas. That's why, Diet Pepsi has been around for 20 years, and it has spent most of that period building a feminine image. But since diet Coke was only a year old when it added NutraSweet, it could quickly change gears and cultivate male drinkers, telling them to drink diet Coke "for the taste of it."

Now, Herbert is quickly hiking up Coke's marketing budget, so consumers are sure to hear plenty more about the brand. And if TV viewers already have a touch of battle fatigue, they might consider this: The high season for soft drinks, and the summer offensive in the cola wars, are still months away.

By Scott Ticer in Atlanta

There should be more to global corporate banking than good deals



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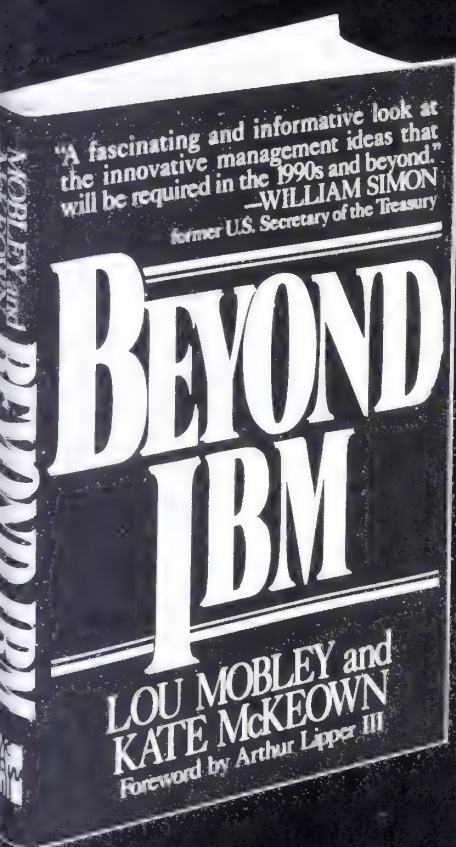
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TAXPAYER-FRIENDLY SOFTWARE THAT ALMOST DOES IT ALL

It's that time again. And this year you've decided to fill out all those tax forms yourself. But if you've been using a spreadsheet or one of the many personal financial management programs on the market to keep track of your finances, there's more reason than ever to draft your PC for the job of sorting through the jumble of numbers and producing a correct and coherent tax return: It can make filing your taxes as easy as 1-2-3.

That's because the programmers who write tax-preparation software are starting to snuggle up to the folks who bring you financial-management packages. Their combined efforts make it possible to electronically pluck the numbers you need from your computer and plug them

into a tax program—without retyping the data. So if you keep tabs on household or small-business finances with an IBM-type PC, and the program or spreadsheet you use can "export" so-called ASCII files, you can "import" those numbers into Ask Dan About Your Taxes and save a lot of time and fuss.

Ask Dan was our top-rated tax program in 1988, and it's even better this year (\$90 from Legal Knowledge Systems at 800 338-1866). The best-selling TurboTax (\$75 from ChipSoft at 800 782-1120) has a similar import link that's new for the 1988 tax year.

Users of Quicken, a \$50 financial-management package

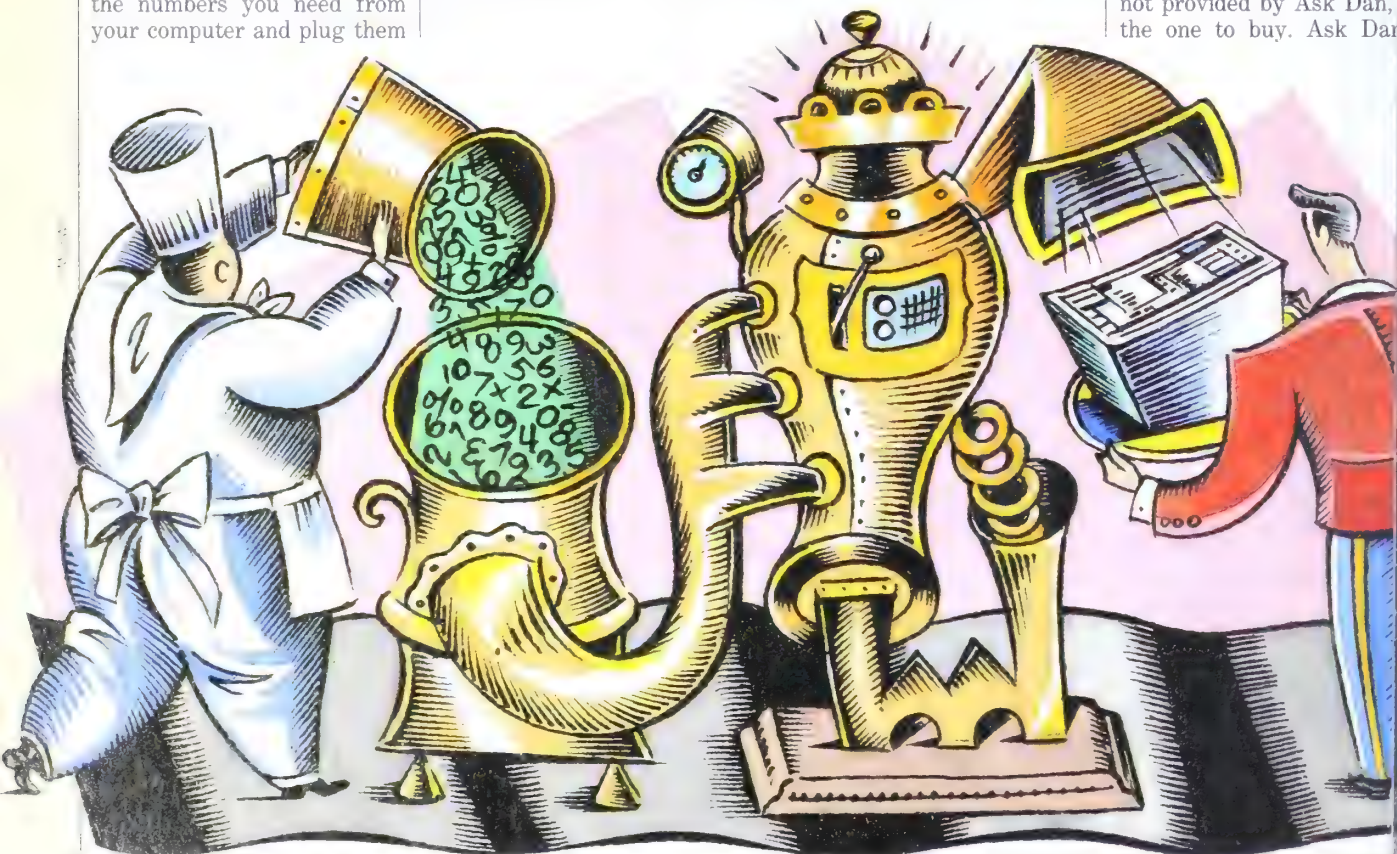
from Intuit Inc. that regularly shows up on software best-seller lists, can export data to either Ask Dan or TurboTax—or to J. K. Lasser's Your Income Tax (\$75 from Simon & Schuster Software at 800 624-0023). While Lasser isn't as pleasant to use, it calculates more tax forms than most tax-preparation programs (chart).

Slickest of all, in terms of the ease with which numbers can be traded between software, is the piggyback arrangement between Andrew Tobias' Managing Your Money (MYM) and its new sidekick TaxCut (\$80 from Meca Ventures at 203 226-2400). Meca's MYM (\$220) is perhaps the most comprehensive personal-

finance program. Because MYM keeps track of just about everything needed for a return, you'd think that integrating a tax-prep routine would be a snap. It wasn't.

FREE ADVICE. So Meca approached Best Program, which was having difficulty doing the reverse—exploiting the popularity of its PC/TaxCut program to sell a financial-management package. Meca proposed they join forces. The result is a program that almost automatically fishes through MYM and extracts the data needed to out IRS forms.

All four tax-preparation programs can also be used themselves. But unless absolutely must have a form not provided by Ask Dan, the one to buy. Ask Dan



first tax program to employ artificial intelligence—a system that knows the ins and outs of tax regulations. Written by Daniel Caine, a young tax attorney who died a lawyer's life wasn't him and founded Legal Knowledge Systems, Ask Danes beyond rehashing IRS

Based on your answers to a questionnaire that comes up when you start the program, it offers plain-English advice and sometimes even makes solicited suggestions on how to reduce your tax bill. The program is smart enough to catch certain deductions that you may be entitled to have overlooked.

IT ALERT. This year's version includes several enhancements to make tax-return filing still less painful. One

COMPARING THE NEW TAX PROGRAMS

Program	Extra forms and schedules handled*	Investor score**	List price
ASK DAN	R, 4684, 6252, 8582, 8606	C	\$90
J.M. LASSER	R, 3468, 3800, 4137, 4255, 4684, 4868, 4952, 4972, 5329, 6252, 8582, 8606	A	75
TAXCUT	3468, 3800, 4952, 5695, 8582***	C	80
TURNOTAX	R, 3800, 4255, 4684, 4797, 4952, 4972, 6252, 8582, 8598, 8606	B	75

*All handle Schedules A, B, C, D, E, and F, plus Forms 1040, 1040-ES, 2106, 2119, 2210, 2441, 3903, 4562, 4797, 6251, and 8615

**Lower score indicates the program does not automatically calculate certain forms needed for reporting investment gains or losses, such as investment interest expense

***With limitations

DATA: BW

speeds up the preparation job with a technique known as hypertext—"hiding" detailed explanations behind various key words on the screen.

Before you print your finished return, another clever innovation comes into play: The program hunts for the

kinds of anomalies and extremes that IRS computers are programmed to ferret out. Filing such a return increases your chances of being hauled in for an audit.

Rather than printing and mailing your return, taxpayers in most states can now

send the data to the IRS via a phone link—as long as they don't owe any money. However, that requires separate software, plus an identification number from the IRS. It may be a little late for that. Instead, you can save your return on a floppy disk and have a local tax-preparation office relay it for you. The cost probably will be \$25 or more, but it will get your refund check in the mail three weeks sooner.

Even without electronic filing, using a computer at tax time should hasten the processing of your return. According to the IRS, one-fifth of all returns are delayed because of taxpayer errors, usually simple ones of addition or subtraction. A tax program isn't likely to make such a mistake.

Otis Port

Finances

THINK RATES MAY EXPLODE? BUY A SHIELD

Following the recent upward trajectory of the prime rate has been a painful exercise for business. Any, if not most, small and medium-size companies borrow at floating rates that are pegged at a fixed number of points above the prime, or have some other common instrument such as the London Interbank Offered Rate, or LIBOR. Over the past 12 months the prime has surged 3.5 points, to 11.5%.

But small companies no longer have to be as vulnerable as they were during the such dramatic surge of short-term rates which took place in the early 1980s. Banks and Wall Street firms, providing interest-rate protection for \$325 billion of borrowings by big companies, are now adapting the big-ticket services to "middle market" customers. The most common of these services are "caps" and "collars."

Caps simply put a ceiling on

the interest rate of an adjustable-rate loan; collars do the same thing, but set a floor rate, too. Of course, like any kind of insurance, interest-rate protection doesn't come free. Caps currently cost around 0.5% of the loan. Collars always cost less because the customer agrees to give up further interest-rate savings if rates fall below the floor.

BETTER PLANNING. John Rigg, chairman of Redco Foods, U.S. distributor of Red Rose tea, says the company bought a collar from Chemical Bank last year to help finance its purchase of Salada Foods. "Right now buying the collar looks like a smart decision," Rigg says, adding that if rates stay the same throughout 1989, Redco will save about \$230,000 in interest expense.

Even if rates don't rise after shelling out premiums for caps or collars, fixing the upper range of borrowing costs adds more certainty to strategic planning. Because Redco is a commodity business, "we do everything we can" to reduce the risks that are not

related to tea, Rigg says.

Glenn Picou at Citibank offers an example of a real estate developer who in September borrowed \$10 million for two years at a rate pegged to

for 11 basis points, or \$11,000. Under the collar, the developer foregoes any chance of benefiting from the prime falling below 9.5%.

The developer felt strongly that rates were headed skyward, so he bought the cheaper collar for one year. Had rates stayed the same, he would have been out that premium of \$11,000. But the way the prime has surged, he's well ahead for having bought the collar. The customer, Picou says, is also concerned that the prime may reach 12% or above in the second year of the loan, jeopardizing his project. He didn't buy coverage for the second year, and now that rates are going up, so are the prices of caps and collars.

The solution? Yet another form of protection. For \$11,000, Citibank sold the developer a "caption"—the right, or option, to buy a 12% cap for a set price of \$45,000 during the second year. That way, for a fraction of the cost of a straight cap, the developer is able to limit his interest-rate risk.

David Zigas



the prime, which then stood at 10%. A cap for the loan at that rate cost a onetime fee of \$30,000—that's 30 basis points, or 0.3% of the loan. Citibank also offered a collar

Smart Money

DON'T DITCH YOUR OLD CD JUST FOR SOME SEXY YOUNG RATE

With interest rates climbing, you may be thinking of moving money out of an older certificate of deposit paying, say, 6% and into a newer CD paying 8%, 9%, or higher. You may even be tempted to shrug off repeated warnings about "substantial penalty for early withdrawal." But there's good reason to do some calculations: The interest rate on your new CD may have to be far higher than you might think to make switching worthwhile.

Most banks and S&Ls charge three months' interest if you close out a CD with a maturity of one year or less, six months' interest on one due to run more than a year. Your first move should be to get clear on your par-

into a new CD gives you more or less interest than you would get by staying put.

An example? Assume \$10,000 was invested a year ago in a 36-month CD paying 7.75% and that a new 24-month CD pays 9.3%. With compounding, the money in the original CD would earn \$2,510 over the 36-month period. You've already accrued \$775 in interest, leaving \$1,735 for the remaining 24 months. The original \$10,000 would earn \$1,946 if invested in a new CD for the next two years. After forfeiting six months of interest as a penalty—at about 0.62% per month, or \$380—you're left with \$1,566.

SIT TIGHT. The question then becomes: Is \$1,735 less than \$1,946 minus \$380? Obviously not—it's best to keep that 7.75% CD for the remaining two years.

Still, by figuring increasingly higher interest rates into the calculations, you can gauge what's needed to come out clearly ahead. In this case, you would need a new two-year CD earning at least 10.4%, so the interest you'd get will be roughly \$2,190. That sort of return still seems fairly far off, but the way interest rates have been acting, it's good to be prepared.

There is another alternative: You could sell your CD on the secondary market where its value rises or falls depending upon current interest rates. With rates up, you won't get full face value, but chances are you'll end up with more than you would if you'd accepted the bank's interest penalty. The problem is, the secondary market usually applies only to jumbo CD's (\$100,000 and up) or those sold through brokerage firms.

Don Dunn

Here's how to figure what it will take to come out ahead

ticular institution's penalty regulations. Some even hold back nine months' interest on a three-year CD, and a year's worth on ones with longer maturity.

But take an instance where you invested in a three-year CD six months ago at something over 7% and now are bombarded with ads proclaiming that current two-year CDs pay better than 9%. What's your move?

To decide, you'll need to know three things: the interest remaining if you hold the CD to maturity, the reinvestment interest the funds would earn in a new higher-rate CD for the time period remaining on the original CD, and the penalty for early withdrawal. The objective is to see if putting the funds



LOW-E GLASS WARMS IN WINTER AND COOLS IN SUMMER

Home

HIGH ENERGY BILLS CAN BE GONE WITH THE WINDOW

If drafts from your home's old windows have been (or caused) a real pain in the neck this winter, now's the time to start thinking about replacing them. It can't be rushed: In this high-tech era, there's more to windows than yesteryear's wooden frame and glass affairs. One major manufacturer has 8,000 sizes, variations, and prices.

Expect to pay about \$175 for a standard double-hung insulating window that has a cold-resistant layer of air between its twin panes. But for \$15 to \$25 more, the inner pane can be Low-E energy-saving glass, which helps cool the house in summer and warm it in winter. Want a tint to filter ultra-violet rays? Tack on another \$15.

Compared with an ordinary pane of glass, double-glazed windows cut heat loss almost in half. "Our standard is one-half inch of air space, and the larger the better," says a spokesman at Marvin Windows. Wide-frame picture windows can be made with an inch or more space. Or you can have windows with argon gas sealed between the panes. Heavier

than air, the invisible, inert gas is a better insulator. There's triple-glazing, too, and the energy savings seldom justify the extra price.

RIGHT SLANT. Low-E glass, on the other hand, soon pays for itself in lower heating bills. Particles of lead and silver in the glass are angled to reflect heat away from the house in summer. In winter, when the sun is lower, they let the warmth radiate inward.

Maximum insulating efficiency involves both glass and frame. A wooden frame insulates better than a metal one, but it requires painting. To avoid the chipping

and choose frames with wood interiors and outer surfaces of vinyl. Extruded aluminum with a baked-on finish.

Brochures are available from among others Andersen (800-255-2550), Marvin (800-346-5111) and Pella (800-628-1000). Both Andersen and Marvin sell through lumber yards and hardware stores which typically offer sales counts; Pella operates its own chain of window stores. Installation can easily double the cost.

D. F.



I lassoed him on Rodeo Drive.
And he drinks Johnnie Walker."



Good taste is always an asset.™



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'Spring training"—try to think of a more evocative phrase in all of sport. Can there be a stronger declaration that better days are coming than the first crack of bat against ball? Throw in the March sunshine of Florida and Arizona, and spring training makes for a great preview of summer.

But if you're contemplating such a break, you'd better get moving. The days of flying in, walking up to the ticket window, and getting a good seat are all but over. Paid attendance in the four-week seasons of the Grapefruit and Cactus leagues has nearly doubled since 1982, to 1.9 million. Hotel space is tight.

NO SWEAT. You can get a road map and a game schedule from the Baseball Commissioner's Office (212 371-7800). For detailed information on the ballparks, there's *Spring Training* magazine or the *Grapefruit League Road Trip* guide by Red Sox broadcaster Ken Coleman. With luck and careful coordination, you can work in as many as 12 teams in a long weekend. At a more leisurely pace, you will have fallbacks: If the Twins' 1:35 game is rained out in Orlando, there's plenty of time to make the 7:05 Reds game in Plant City. There you'll not only find Pete Rose but also a strawberry festival.

That's one of the charms of spring training—the small-town intimacy that's almost uniformly absent in the concrete domes and bowls up North. In Lakeland, Tigers' owner Tom Monaghan marks St. Patrick's Day with green bases and uniforms. And in Bradenton, the ramshackle feeling of McKechnie Field makes Pirates games seem like a day at the county fair.

There are, of course, some negatives. Arrive late at the

Leisure

TOUCHING BASE WITH THE BOYS OF SPRING



Blue Jays' camp in Dunedin, and you won't be able to find a place to park. Visit any of the six teams along Florida's I-4, and you can be tied up with Disney World traffic. If your team is on the road, you might get a lineup of rookies and scrubs. And a few of the newer parks have taken away the old intimacy between the players and the fans: The Mets' home in Port St. Lucie

is a miniature Shea Sta-

But even in the hand- less inviting parks, spring training is the best way to see the stars of tomorrow now, fans everywhere will see the Mets' hot-hitter Gregg Jeffries. But the young players have significant great potential. In Mesa, the Cubs have three could-be perstars: pitcher Mike Bielecki, whose fastball can reach 100 mph, quick-footed fielder Jerome Walton, and the batting champ of the year's U.S. Olympic team, Griffin. In the town now officially called Baseball, Fla., the Royals have Gordon, who rose through the minors last year by striking out 263 batters in only 11 innings. And the Brewers' star in suburban Phoenix has Sheffield, who bolted the last year's season line-up young Willie Mays.

Then there are the old-timers, the big leaguers, those fine players who made their mark in the past. The Yankees' slugger, Fort Lauderdale's star, have two sub- tables: To

John, and Guidi And

Pirates camp, in Stennett, who was forced into retirement five years ago. A broken leg, is now for a comeback.

For them are the rookies hoping to knock them off. a chance to live the dream of the hood. And what training about, is

Ray Ho

Stop and smell the rosin as superstars such as Oakland's McGwire loosen up

Worth Noting

■ FLASH CASH. Answering a youngster's plea to "send money" is now simpler. American Express is expanding its MoneyGram service to major cities in Europe,

Asia, and Australia. From domestic offices (locations, 800 543-4080) you can wire \$100 to \$10,000 abroad for a fee of \$25 to \$350. On most sums, the price undercuts that of competing services.

■ GETTING A GRIP. At 3.3 pounds, Canon's new top-of-

the-line camcorder has two sets of controls for recording and zooming: one set if you want to grip it one-handed like a regular camcorder, another if you prefer to hold it with both hands like a 35mm camera. The high-definition 8mm goes for \$2,300.

■ MBA CHANNEL. Next to 100 cable-TV systems with Colorado State University lessons for college graduates who want to earn an M.B.A. The 33-credit program costs about \$10,000 and can be completed in three years. Details: 800 777-6463.



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Conference Calls

Strategies For Effective Meeting Planning



Among the tens of thousands of meetings conducted every year are a large number put together by a corporation or association executive who has never before planned one. There are a great many ways in which such a scenario can develop, and all of them can lead to panic. But if you're in this spot, don't worry. Help is only a phone call away.

And at the other end of the wire are representatives of hotels, airlines, travel companies and a host of other suppliers. All of them are experts.

Before you make your first call, there are two things you ought to know.

First, what kind of a meeting do you want? Any information you can turn up on previous similar meetings—attendance counts, menus, programs, whatever—will prove immeasurably helpful.

Strategies For Effective Meeting Planning

Second, you'll need a set of phone numbers. If for some reason you can't call last year's suppliers, your business associates or a professional association often can provide leads, and once you've made your first contact or two, others will follow naturally.

But if you really want to plan a meeting with as little fuss as possible, you should understand what these various suppliers can and cannot do for you. What follows are a few basic guidelines.

CONVENTION AND VISITORS BUREAUS

One of the most important calls you can make is to a convention and visitors bureau or CVB. (In some cities this organization is called by a

slightly different name, convention and tourism association, for example.) CVBs can help you select your site. They will gladly send you detailed dossiers on meeting facilities, restaurants and entertainment options. *The San Francisco Facilities and Services Guide*, for example, is 144 pages and offers plans of the city's major meeting halls as well as 18 entries under "Restaurants That Cater." Chicago's guide includes five entries under "Candy Stores."

Someone from the CVB assigned specifically to your group can help you plan a site-inspection visit and even may show you around. Such trips seldom last longer than a night or two, but they are invaluable. You will learn the specifics of properties and the general lay of the land. Of course, the attention you get from a CVB depends, to some extent, on the size of your group.

CVBs also can assist you in locating venues for your special events and can inform you of other

events scheduled for the dates your group will be in town. They often can tell you what hotels have availability on your dates and pass on your specifications to hotel sales departments.

Like the airlines, CVBs can provide you with promotional materials (photos, brochures, etc.). If you're holding a convention, they can provide experienced registration personnel.

What CVBs won't do is get involved in your negotiations with hotels and meeting facilities or other suppliers. Nor will they be intermediaries for your financial transactions. Theirs is strictly an advisory role.

AIRLINES

If ten or more people will be attending your meeting, an airline will refer you to its group department (this may be called by a number of names) and an airline representative will be

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TWA

Strategies For Effective Meeting Planning

assigned to you. Your "rep" can provide you with an analysis of the costs involved in reaching different destinations.

An airline also may fly you to inspect sites. If your passengers are coming from different directions, the airline can set up special reservations procedures. No matter what the size of your group, the airline computer should be able to provide you with a complete breakdown of arrivals and departures for your participants.

If your group is over 100 or 150 people, an airline may be willing to offer a special fare. These fares will generally be one-third to one-half off the cost of a regular coach ticket or a few percentage points lower than the cost of an advertised Supersaver.

Airlines also can give you promotional assistance. They may provide literature on your destination and "shell" brochures carrying general information onto which you print the specifics of your program. If



Planning with the fewest possible calls means knowing what suppliers can and cannot do.

you wish to print your own brochures, an airline may be willing to pick up part of the cost. Also, airlines sometimes will give away tickets to be used in promotional contests or buy ads in association magazines to

help build attendance.

As your meeting approaches, an airline usually will ship materials (meeting programs, audio-visual equipment, computers, etc.) to your destination for free. And an airline also will provide "earned" tickets for your staff or VIPs on a ratio of somewhere around one per 25 to 40 paid passengers.

HOTELS

When you call a hotel, someone with a title like "convention sales manager" will be assigned to your account. The first thing he or she will do is advise you on the availability of room space. If you have indicated that your dates might be flexible, your sales manager may suggest alternate dates for which the hotel can give you better rates.

For a meeting of any substantial size, your sales manager usually will give you a complimentary room so you can come and inspect the property. During that visit, you will be introduced to the hotel's department heads.

Your sales manager will send you diagrams of the hotel's meeting room layouts and estimates on the cost of each of your functions. Some major hotels have special procedures for smaller groups in which the sales manager on the account also helps execute the event itself. At most hotels, however, your group eventually will be turned over to someone with a title like "convention services manager."

Your convention services manager will analyze the functions requested and make up a master plan. He or she will stay in touch with you, keep track of your attendance projections and inform you of any changes by the hotel. He will also reserve the proper audio-visual equipment. And he will advise you on where to get special banners, promotional items, name badges, etc.

What hotels don't usually do is get involved in the protocol or the programmatic aspects of your meeting.



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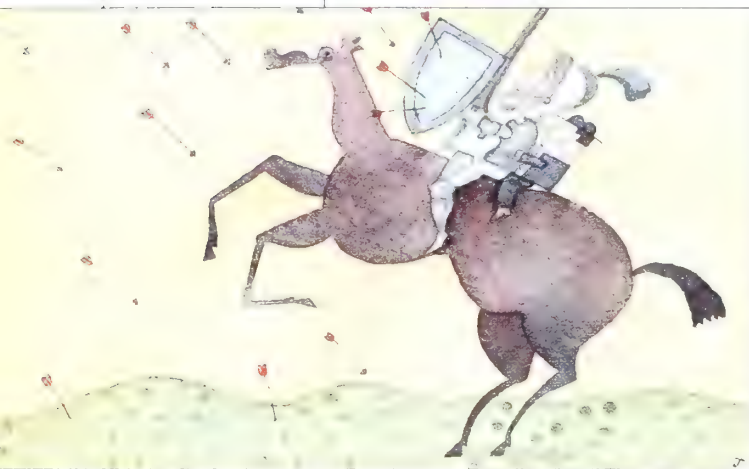
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Strategies For Effective Meeting Planning

DESTINATION MANAGEMENT COMPANIES

Unless your group is very small or your program very simple you will probably be hiring a destination management company or "DMC." You just may not know it at first.



DMCs provide an important shield against the slings and arrows of outrageous meeting fortune.

DMCs contract for ground transportation, handle transfers, provide meet-and-greet service for arriving VIPs, arrange off-site tours and events, assist with on-site special events, put together spouse programs, and much, much more. (A few are even licensed to write air tickets.)

The quality of an event can't be measured by its cost per head. Some DMCs, like some hosts, add life to the party. There are DMCs that specialize in off-the-beaten-path art, architectural or shopping tours, but even more important than the creativity of a DMC's pre-arranged offerings are the ideas it can come up with on the spot. For example, Myla Lerner, vice-president of Tours West, Mill Valley, Calif., recalls the time two delegates from Beijing showed up

unexpectedly at a convention. She wowed them with a visit to something they could never have seen in China: a giant supermarket.

DMCs also can provide good local speakers, photographers, special pillow gifts, translators, and a host of other services. Their intimate knowledge of their locales will prevent you from booking your group into, say, a restaurant whose service has gone downhill—or from scheduling a tour that will leave your group too tired to enjoy the evening's events.

What DMCs generally won't do is have any involvement with your air arrangements beyond picking up your passengers at the airport and returning them. Nor, generally speaking, will DMCs handle hotel bookings.

INDEPENDENT PLANNERS

If you want to plan a meeting with only one call, make that call to an independent meeting planner. These professionals become what Marilyn Hauck, president of The Complete Conference, Sacramento, Calif., calls "the common denominator in a highly complex equation." They can do something no one else will: get involved with your program.

Independent planners will help you to achieve your programmatic objectives from a conceptual as well as a logistical standpoint. They can help you analyze your meeting message and discuss ways of getting it across. For this reason, one of the best ways to work with an independent planner is to start on a consulting basis. If you find that you like your planner's ideas (or that your planner has good suggestions for implementing *your* ideas), you then can give him operational responsibilities.

Independent planners won't, generally, handle payments for travel companies or hotels, but they will help you locate and work with those suppliers. "Most of us have phenomenal networks," says Joan Eisenstodt, a planner based in Washington, D.C.

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Strategies For Effective Meeting Planning

RENTAL CAR COMPANIES

The meetings services provided by rental car companies are basic but nonetheless valuable. First, they often will negotiate a discounted rate (perhaps 10-15% below standard) for your group. Then, they will establish special reservations procedures (usually through an 800 number) and provide materials with which to inform your participants of these procedures.

Rental car companies also will offer a small number of complimentary cars on a basis of about one per 25 rental cars.

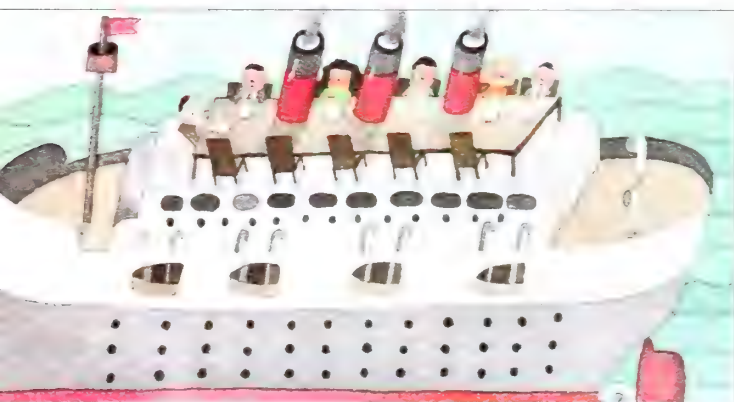
CONFERENCE CENTERS AND CRUISE SHIPS

Conference centers and cruise ships both offer self-contained environments. This is important if group solidarity is one of your meeting's main goals.

While there are conference centers that double as resorts, most offer a quiet, almost monastic environment, albeit one with all the latest conferencing amenities. They are best for the intensive training seminars and strategic planning sessions only infrequently attended by spouses.

By contrast, only a few cruise ships are outfitted with extensive meeting facilities, and most meetings at sea are more social and limit sessions.

On the other hand, a special spirit can develop on a cruise. "Ninety-eight percent of the meetings we do have spouses along," says Cherie Miller, director of group and incentive sales for Carnival Cruises, "and a lot of internal networking goes on—a real camaraderie develops."



Cruise ships offer a self-contained meeting environment & a unique setting for social functions.

TRAVEL COMPANIES

There are good reasons to call a travel company, but before you do, make sure you know what type of outfit you're calling. Try to find one that specializes in corporate travel or, better yet, in meetings or incentive travel.

Frequently, travel companies have "preferred vendor" status with some suppliers. Thus, even if your company or association meets only once a year, your travel company will be given the special attention due a regular customer.

Also, travel arrangers can assess a destination's cost as a total package, not just in terms of air fares or hotel rates. For example, Steve Damerow, national marketing manager for Osborne Incentive, Atlanta, says, "I can sometimes put together a meeting in Cancun (Mexico) for less than I can in Atlanta."

And a travel company will save you time. It will lighten the burden by taking reservations, making changes and keeping track of rooms, arrivals and events sign-ups.

Some of the larger meeting and incentive houses can not only ship state-of-the-art audio-visual equipment to your site but can help put together your presentation.

Strategies For Effective Meeting Planning

Once you and your planner have agreed on concepts, your planner will draw up a time-line chart, establish performance criteria and, if necessary, help you train your in-house staff to perform necessary meeting functions.

When your event actually takes place, it is your planner who will lose sleep double-checking every room set-up and audio-visual system, leaving you free to interact with attendees and VIPs. "Our job," Eisenstodt says, "is to stay behind the scenes and make somebody else look good."

Your planner will continue working on your meeting even after it's over by sending thank-you notes and gratuities in your name and by evaluating the performance of your suppliers and reconciling their charges.

IN CONCLUSION

There is a considerable amount of overlap in the meetings field. The same meeting-room set-up can be specified directly to your hotel or requested through your DMC, travel company or independent meeting planner. In the end, it is you, the meeting client, who must establish priorities and make the final decisions.

Still, it's the first decisions that are likely to be the most important. Those are the decisions on who you want on the other end of the phone helping you. If you can make a few good choices, there's so much expertise available that everything will get easier from there. ■

Conference Calls: Strategies for Effective Meeting Planning has been prepared by the editors of *Meeting Destinations* magazine. Editorial Director, Julie Moline; Executive Editor, Linn Varney; Designer, Jeanine Dunn; Writer, Jeremy Weir Alderson; cover and illustrations, John Segal

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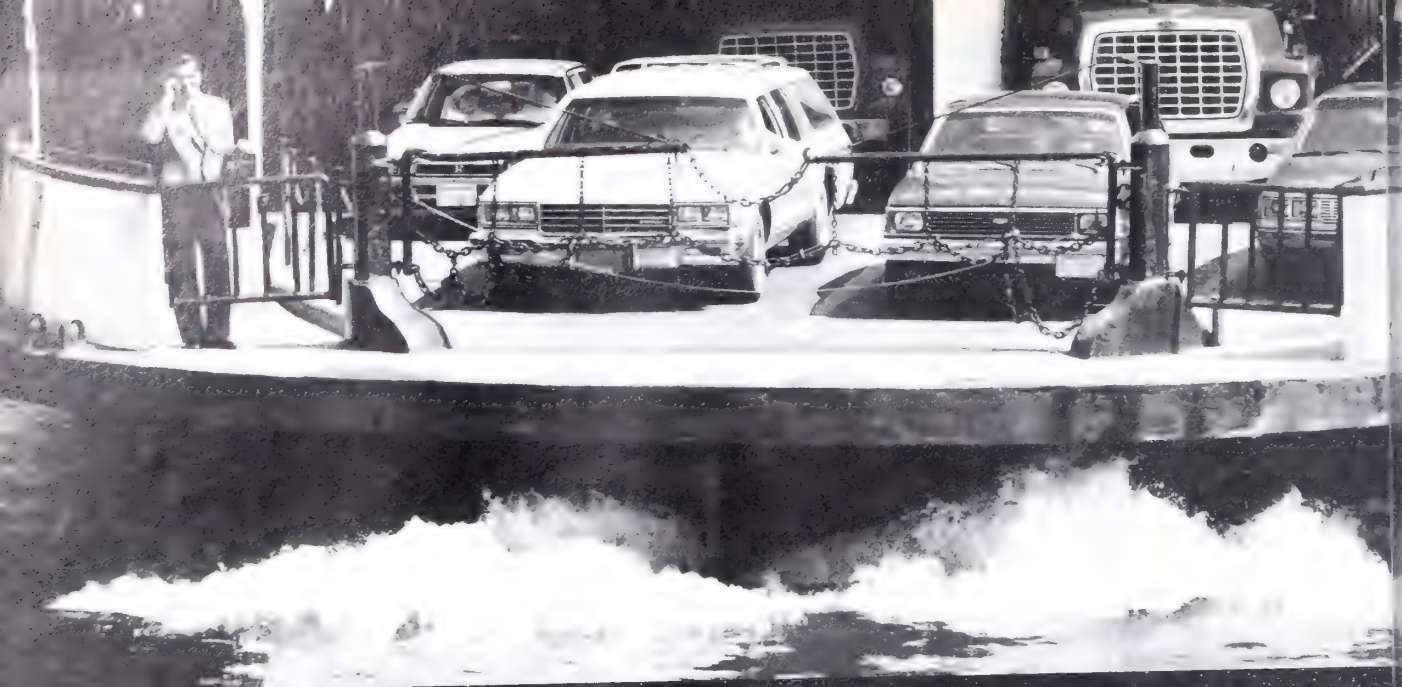
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Wickes 54
Wyatt 126
Y
Yamaichi 140

1	Exxon
2	General Motors
3	Mobil
4	Ford Motor
5	IBM
6	Texaco
7	E.I. du Pont
8	Standard Oil (Ind.)
9	Standard Oil of Cal.
10	General Electric
11	Gulf Oil
12	Atlantic Richfield
13	Shell Oil
14	Occidental Petroleum
15	U.S. Steel
16	Phillips Petroleum
17	Sun

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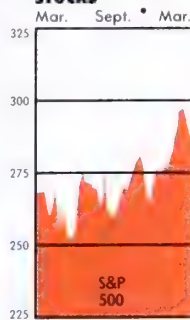
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Investment Figures of the Week

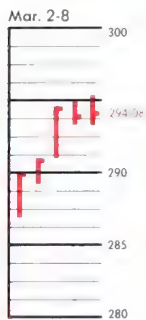
COMMENTARY

Stock market, fretting over inflation and higher interest rates last week, found good reason to cheer. The megamerger between Time Inc. and Warner Communications Inc., announced on Mar. 5, generated a wave of excitement and gave investors hope that another round of stock market mania was starting. Most stocks ran up, and small companies joined the party along with blue chips. Little changed in the bond market, as traders awaited new economic data.

STOCKS

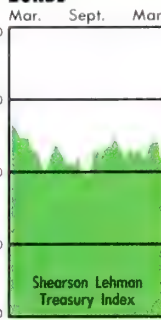


52-week change
+9.3%



1-week change
+2.4%

BONDS

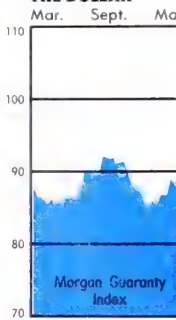


52-week change
-5.0%

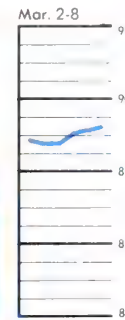


1-week change
+1.1%

THE DOLLAR



52-week change
+3.7%



1-week change
+0.4%

MARKET ANALYSIS

STOCKS

	Latest	% change Week	% change 52-week
DOW JONES INDUSTRIALS	2295.5	2.3	10.7
DOW JONES COMPANIES (Russell 1000)	155.7	2.2	9.2
DOW JONES COMPANIES (Russell 2000)	157.9	2.1	11.4
DOW JONES COMPANIES (Russell 3000)	167.3	2.2	9.3

FOREIGN STOCKS

	Latest	% change (local currency) Week	% change (local currency) 52-week
DOW JONES FINANCIAL TIMES 100	2083.3	3.1	14.8
DOW JONES NIKKEI INDEX	31,837.7	-0.4	24.3
DOW JONES TSE COMPOSITE	3632.5	2.3	8.9

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	8.6%	8.6%	5.7%
30-YEAR TREASURY BOND YIELD	9.1%	9.2%	8.5%
S&P 500 DIVIDEND YIELD	3.4%	3.3%	3.1%
S&P 500 PRICE/EARNINGS RATIO	11.9	11.6	15.5

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 26-week moving average	279.6	278.5	Positive
Stocks above 26-week moving average	61.7%	59.1%	Neutral
Speculative sentiment: Put/call ratio	0.24	0.30	Negative
Insider sentiment: Vickers sell/buy ratio	1.14	1.15	Positive

INDUSTRY GROUPS

4-WEEK LEADERS

	% change 4-week	% change 52-week
ENERGY	13.4	41.3
OIL AND GAS DRILLING	11.0	-4.7
ENTERTAINMENT	9.6	32.0
OIL WELL EQUIPMENT AND SERVICES	8.8	5.4
HEALTH CARE SERVICES	7.8	-41.5

4-WEEK LAGGARDS

	% change 4-week	% change 52-week
MINING	-9.4	0.4
MACHINE TOOLS	-7.3	-10.0
SEMICONDUCTORS	-6.2	-16.9
CRITICAL EQUIPMENT	-5.8	-1.8
SHIP CONTAINERS	-5.7	20.3

Strongest stock in group

	% change 4-week	% change 52-week	Price
HASBRO	20.6	41.1	19 3/4
ROWAN	12.5	-8.5	6 3/4
WARNER COMMUNICATIONS	16.0	51.0	48 7/8
BAKER HUGHES	19.0	8.7	17 1/4
BEVERLY ENTERPRISES	26.3	18.0	9

Weakest stock in group

	% change 4-week	% change 52-week	Price
CONSOLIDATED FREIGHTWAYS	-16.4	1.7	30 1/2
CINCINNATI MILACRON	-9.1	-10.5	22 3/8
ADVANCED MICRO DEVICES	-13.3	-33.0	8 1/8
AMP	-8.3	-14.3	44 1/8
STONE CONTAINER	-9.2	22.4	32 1/8

BRIDGE INFORMATION SYSTEMS INC.

MUTUAL FUNDS

LEADERS

	% 4-week total return
STRATEGIC INVESTMENTS	6.0
UNITED SERVICES GOLD SHARES	5.7
HEALTH MONITORS	4.7

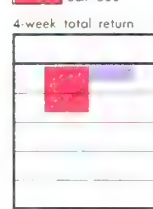
LAGGARDS

	% 4-week total return
ALLIANCE TECHNOLOGY	-7.7
FIDELITY SELECT COMPUTERS	-5.4
FIDELITY SELECT SOFTWARE & COMPUTER	-5.2

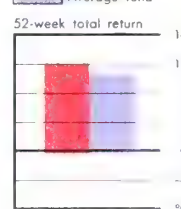
	% 52-week total return
STEFAN MANN	53.7
ALLIANCE GLOBAL CANADIAN	36.9
COLUMBIA SPECIAL	35.9

	% 52-week total return
STRATEGIC INVESTMENTS	-27.3
STEADMAN OCEANOGRAPHIC TECHNOLOGY	-19.9
UNITED SERVICES GOLD SHARES	-19.0

S&P 500



Average fund



MORNINGSTAR INC.

RELATIVE PORTFOLIOS

Amounts sent the present of \$10,000 after one year in each portfolio

	Foreign stocks	U. S. stocks	Money market fund	Treasury bonds	Gold
Amounts sent the present of \$10,000 after one year in each portfolio	\$12,559	\$11,202	\$10,648	\$10,057	\$9,049
Pages indicate by total returns	-1.02%	+1.73%	+0.16%	+0.50%	+0.97%

DATA RESOURCES INC.

On this page are as of market close Wednesday, Mar. 8, 1989, unless otherwise indicated. Groups include S&P 500 companies only; performance and share prices are as of market close.

Mar. 7. Mutual fund returns are as of Mar. 3. Relative portfolios are valued as of Mar. 7. A more detailed explanation of this page is available on request.

TWO LABOR LAWS ARE ONE TOO MANY

The machinists strike at Eastern Airlines may touch off a big labor battle in Congress—but over an issue that is much narrower than the real problem. If the International Association of Machinists (IAM) sets up picket lines at railroads and other airlines, President Bush will demand that Congress amend the Railway Labor Act—which covers airline and railroad employees—to outlaw secondary picketing. The government's concern about widespread travel disruptions is understandable. But a better solution would be to dismantle the RLA, along with its obsolete strike-avoidance procedures, and transfer airline and railroad workers to the National Labor Relations Act, which covers all other private-industry employees.

The fact is that this dualism in federal labor law creates two classes of workers and employers, with different rights and duties. Under the NLRA, workers are prohibited from engaging in secondary picketing, while the RLA allows it. But an equally significant difference arises out of provisions governing collective bargaining. The 1935 NLRA encourages "good faith" bargaining but for the most part stands aside and lets the two sides fight it out. The government intervenes only in cases of national emergency.

The purpose of the RLA, on the contrary, was to use the powers of the government to prevent strikes by union members. Back in 1926, when the act was passed, big rail strikes could disrupt the national economy. But the RLA's cumbersome provisions, including conciliation by the National Mediation Board and numerous meaningless deadlines, permitted endless stalling. These procedures are largely responsible for the mess at Eastern and actually impede collective bargaining. Thirteen months lapsed before the NMB declared an impasse in the IAM-Eastern talks, and some bargaining rounds have lasted much longer.

The protracted negotiations at Eastern allowed by the NMB also have been criticized by Frank Lorenzo, chairman of Eastern's owner, Texas Air, but his confrontational tactics in dealing with unions only serve to damage the process.

Even after the NMB's procedures have been exhausted, the President may delay a strike for 60 days by appointing an emergency board to recommend a settlement, which either side may reject. At that point, Congress normally steps in and mandates the settlement terms. The undesirable result is collective bargaining by edict.

THE MOMMY TRACK: A QUESTION OF CHOICE

In an ideal world, perhaps men and women would share the workplace and the home equally, and corporations wouldn't discriminate against child rearers, be they men or women. Some feminists have used this argument to oppose setting up the so-called mommy track, the search for

new ways to balance career goals and mothering (p. 126)—a human place to stand, if you will, between superwoman and June Cleaver. But in the real world a woman's career can't always look just like a man's.

Faced with a choice between the fast track at work and raising a family, many mothers of small children will opt out. These career women pose a special problem for corporations, which is faced with a choice: Either develop a flexible working pattern for them or lose them. However unsettling this plan may be to corporate chauvinist and equality purists, there should be a mommy track for those who want it or have no alternative. Those who don't want to take this option can try to have it all. In short, we need to have many different, flexible tracks—not just a stark choice of staying home or working full time. And choosing to step down for even a few years should not derail a career.

In addition to the human reasons for providing flexibility in the workplace, there is an equally compelling economic reason. Women are a very large part of our human capital, and it is nonsense to continue with rigid attitudes toward job-sharing, flexible hours, and other innovative techniques that can allow more women—or men for that matter—to work productively and be a parent at the same time.

LESSONS FROM THE TIME-WARNER DEAL

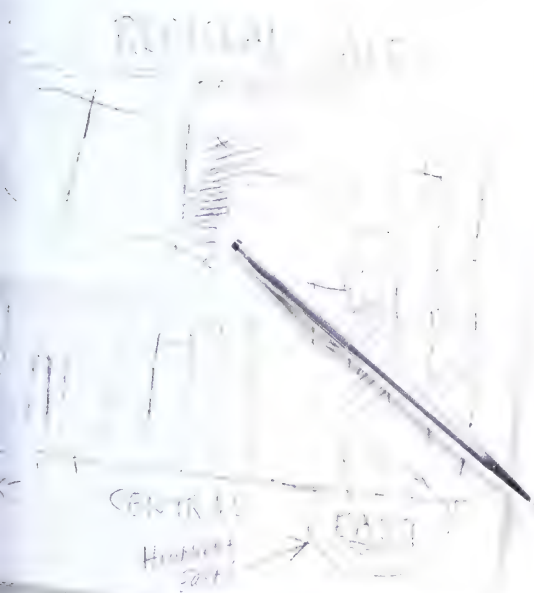
After two years of talks, Time Inc. and Warner Communications have agreed to the largest merger in the media and entertainment industry. The companies believe that the creation of a \$10 billion Time Warner Inc. would create a world-class competitor ready for Europe in 1992 and any other global challenge.

At first blush, the sheer size of the deal may raise eyebrows. But fears about the combination's power seem to have been blown away. Time Warner's cable operations still will be dwarfed by industry leader Tele-Communications Inc. And competition within the entertainment industry will limit the power wielded even by an integrated company with a movie studio, cable systems, and premium cable channels such as HBO and Show Box Office.

The Time-Warner deal does raise some legitimate questions, however. The transaction makes it clear that the media industry finally has grown up. And it's time to take a fresh look at curbs on its competitors. The powerful local print companies, for instance, can't compete in their service areas with cable-TV operators. Policymakers should consider whether cable's monopoly is healthy.

Another pressing issue is whether the networks, whose market share is steadily eroding, should be allowed to produce and syndicate the lucrative prime-time television shows they air. With audiences dwindling and advertising growing slowly, the networks claim that they need the extra revenue from program syndication to cover their costs—and to remain healthy enough to give cable a run for the money. If you're worried about concentration of power at the Time Warner, there's an easy answer: unlock the door to competition.

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March 27

BOOM!
PAGE 76

WHAT THE NEXT RECESSION WILL LOOK LIKE

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IS YOUR COMPANY TOO BIG?

PAGE 84



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Cover Story

84 IS YOUR COMPANY TOO BIG?

Big is better. That's what most executives and stockholders were brought up to believe. But the shibboleth that equates size with success is turning out to be a myth, and many corporate Goliaths now are trying to look and act more like feisty, entrepreneurial Davids

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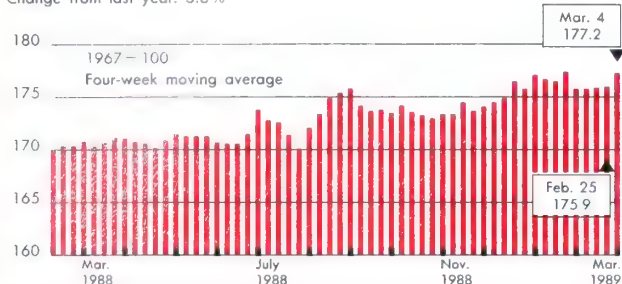
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Big is no substitute for smart
What's wrong with Wright
Hope for cutting Third World debt

BusinessWeek Index

PRODUCTION

Change from last week: 0.7%
Change from last year: 3.8%

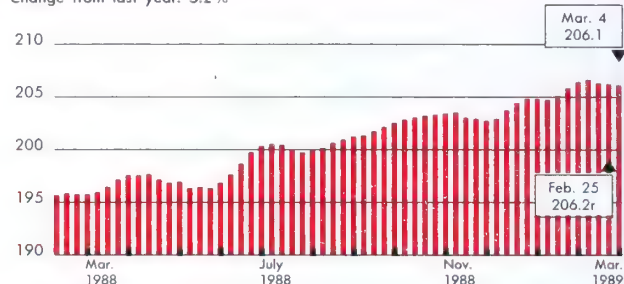


The production index increased for the week ended Mar. 4. On a seasonally adjusted basis, output of autos, coal, rail-freight traffic, paper, paperboard, and trucks increased. Lumber, steel, and electric power production declined. Crude-oil refining output was unchanged from the previous week. Prior to calculation of the four-week moving average, the index also advanced, to 177.8, from 176.7 for the week before.

BW production index copyright 1989 by McGraw-Hill Inc.

LEADING

Change from last week: -0.1%
Change from last year: 5.2%



The leading index declined for the week ended Mar. 4, continuing a downward trend started in mid-February. For the latest week, lower stock prices, higher bond yields, and slower growth in real estate loans offset a rapid increase in materials prices and higher growth in M2. Data on business failures were unavailable. Before calculation of the four-week moving average, the index rose slightly to 206.4 from the previous week's 206.3.

Leading index copyright 1989 by Center for International Business Cycle Research

PRODUCTION INDICATORS

	Latest week	Week ago	% Change year ago
STEEL (3/11) thous. of net tons	2,012	1,956 #	2.3
AUTOS (3/11) units	146,169	153,560r #	5.9
TRUCKS (3/11) units	89,749	93,478r #	4.9
ELECTRIC POWER (3/11) millions of kilowatt-hours	55,640	54,857 #	12.7
CRUDE-OIL REFINING (3/11) thous. of bbl./day	12,791	12,654r #	1.2
COAL (3/4) thous. of net tons	19,793 #	19,398	5.7
PAPERBOARD (3/4) thous. of tons	756.1 #	753.8r	2.5
PAPER (3/4) thous. of tons	762.0 #	753.0r	3.8
LUMBER (3/4) millions of ft.	466.3 #	487.3	-11.8
RAIL FREIGHT (3/4) billions of ton-miles	19.8 #	18.9	3.7

Sources: American Iron & Steel Inst., Ward's Automotive Reports, Edison Electric Inst., American Petroleum Inst., Energy Dept., American Paper Inst., WWPA¹, SFPA², Association of American Railroads.

FOREIGN EXCHANGE

	Latest week	Week ago	Year ago
JAPANESE YEN (3/15)	131	129	127
GERMAN MARK (3/15)	1.87	1.86	1.67
BRITISH POUND (3/15)	1.72	1.72	1.85
FRENCH FRANC (3/15)	6.34	6.32	5.68
CANADIAN DOLLAR (3/15)	1.20	1.20	1.25
SWISS FRANC (3/15)	1.61	1.59	1.38
MEXICAN PESO (3/15) ³	2,371	2,362	2,300

Sources: Major New York banks. Currencies expressed in units per U. S. dollar, except for British pound expressed in dollars.

PRICES

	Latest week	Week ago	% Change year ago
GOLD (3/15) \$/troy oz.	392.900	394.600	-11.9
STEEL SCRAP (3/14) # 1 heavy, \$/ton	115.50	123.00	-2.9
FOODSTUFFS (3/13) index, 1967 = 100	231.2	231.4	7.2
COPPER (3/11) c/lb.	153.9	148.7	40.9
ALUMINUM (3/11) c/lb.	101.0	102.5	-5.6
WHEAT (3/11) # 2 hard, \$/bu.	4.51	4.47	46.4
COTTON (3/11) strict low middling 1-1/16 in., c/lb.	56.68	55.73	-4.3

Sources: London Wed. final setting, Chicago mkt., Commodity Research Bureau, Metals Week, Kansas City mkt., Memphis mkt.

Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment
1 = Western Wood Products Assn. 2 = Southern Forest Products Assn. 3 = Free market value NA = Not available r = revised NM = Not meaningful

LEADING INDICATORS

	Latest week	Week ago	% Change year ago
STOCK PRICES (3/10) S&P 500	293.91	288.98	10.1
CORPORATE BOND YIELD, Aaa (3/10)	9.73%	9.75%	4.2
INDUSTRIAL MATERIALS PRICES (3/10)	104.3	103.8	7.4
BUSINESS FAILURES (3/3)	NA	NA	NA
REAL ESTATE LOANS (3/1) billions	\$313.0	\$312.8	12.6
MONEY SUPPLY, M2 (2/27) billions	\$3,095.6	\$3,090.6r	4.8
INITIAL CLAIMS, UNEMPLOYMENT (2/25) thous.	295	317	-14.2

Sources: Standard & Poor's, Moody's, Journal of Commerce (index: 1980 = 100), Dun & Bradstreet (failures of large companies), Federal Reserve Board, Labor Dept. CIBCR seasonally adjusts data on business failures and real estate loans.

MONTHLY ECONOMIC INDICATORS

	Latest month	Month ago	% Change year ago
EMPLOYMENT, CIVILIAN, MILLIONS, (Feb.)	116.9	116.7	2.3
UNEMPLOYMENT RATE, CIVILIAN (Feb.)	5.1%	5.4%	-10.5
EXPORTS (Jan.) millions	\$37,290	\$40,052	8.9
IMPORTS (Jan.) millions	\$27,802	\$29,062	13.5

Sources: BLS, Commerce Dept.

MONETARY INDICATORS

	Latest week	Week ago	% Change year ago
MONEY SUPPLY, M1 (2/27)	\$789.2	\$789.2r	2.8
BANKS' BUSINESS LOANS (3/1)	312.2	310.0	5.4
FREE RESERVES (3/8)	365	649r	-46.6
NONFINANCIAL COMMERCIAL PAPER (3/1)	110.2	107.9	26.5

Sources: Federal Reserve Board (in billions, except for free reserves, which are expressed for a two-week period in millions).

MONEY MARKET RATES

	Latest week	Week ago	Year ago
FEDERAL FUNDS (3/14)	9.78%	9.59%	6.61%
PRIME (3/15)	11.50	11.50	8.50
COMMERCIAL PAPER 3-MONTH (3/15)	9.87	9.80	6.61
CERTIFICATES OF DEPOSIT 3-MONTH (3/15)	10.00	9.95	6.62
EURODOLLAR 3-MONTH (3/8)	10.03	10.03	6.74

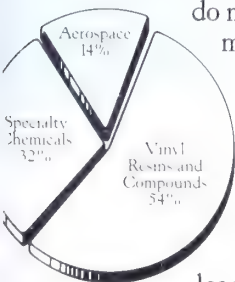
Sources: Federal Reserve Board, First Boston



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A SALVO FROM CANNON'S 'MYSTERY MOGUL'

I was shocked and dismayed to read "Puzzle in movieland: The case of the mystery moguls" (Entertainment, Mar. 13). The article is replete with misstatements and false innuendos that damage not only me but also many innocent stockholders of the entities in which I am a participant.

As an officer, director, and investor in a number of public and private companies throughout the world, including Cannon Group and Pathé Cinema, I am well aware of the legal and ethical standards for the conduct of large-scale international business. I have always held myself and my associates to the highest standards of conduct with respect to our business and financial affairs.

The article makes untrue and baseless accusations of money laundering. Had the editors verified the information before publishing the article, they would have learned that the financial statements of each entity in which I am involved are audited by Peat, Marwick, Main & Co. Although Cannon does not comment on estimates of its earnings (which will be released later this month), the statement of Cannon's 1988 loss bears no relationship whatsoever to reality. Moreover, the suggestion in the article of supposed "close ties with Sicilian crime families" is slanderous and totally false.

In fact, about the only statement in the article that has any basis in fact is that "I want to build the biggest film group in the world." I am dedicated to building a highly credible and successful entertainment-communications business that derives its strength from imaginative, creative management and honest, honorable dealings with the business and entertainment communities.

The irresponsibility of BUSINESS WEEK in publishing an article riddled with false statements and highly damaging innuendos is to be derided in the world of responsible journalism. My record and those of my associates and the entities with which I am affiliated speak for themselves. Based on this record, there is no mystery about my personal integrity or business ethics, and I will not toler-

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ate the irresponsibility of this article which seeks to create such doubts.

Giancarlo Parretti
President and CEO
Cannon Group Inc.
Los Angeles

Editor's note: The loss referred to in the story was an operating loss, before extraordinary gains. As for Mr. Parretti's other comments, we printed his denial in the original story and stand by our reporting.

CLOSING THE TRADE GAP: TOUGH, BUT NOT IMPOSSIBLE

Your story on our trade deficit ("We ever close the trade gap?" Cover Story, Feb. 27) was greatly needed. You point out that depreciating the dollar and cutting the federal budget deficit won't improve the situation. What you fail to note, however, is that U.S. industry must take international competition more seriously by putting more energy into designing better products.

The reason that Nissan cars, Braun coffee makers, and Benetton sweaters are more popular is that they are better designed. The appearance, function, and ease of manufacture of these products are also well designed.

Ford and Xerox recaptured market share by redesigning both the design process and the products. Now their products are well designed for user service, and manufacturing.

Large and small American companies can help to reduce the trade deficit by

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Gen. Mgr. & Secy. Frank D. Penglase, Senior VP, President, Treasury Operations

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ing design not as a short-term visual
etic but as a long-term business strate-
y that addresses a wide range of man-
agement concerns.

Peter Lawrence, Chairman
Corporate Design Foundation
Boston

Your cover story is a sobering analy-
sis of the critical tasks ahead for
r nation. We would point out, howev-
r, that you overlook the importance of
rvice in international trade and their
eat potential for improving the U.S.
sition.

Of particular significance are travel
d tourism, which in terms of export-
nerated employment and expenditures
international visitors are our coun-
y's largest exports. In 1988 tourists to
e U.S. spent more than \$18 billion (not
cluding international transportation)
d generated more than 350,000 jobs.
Nonetheless, in the same year Ameri-
ns traveling abroad spent more than
4.5 billion, producing a net tourism
ade deficit of nearly \$6.5 billion. Even
ore troubling is that our nation's share
the global tourism market has actual-
been declining in recent years.
Part of the problem is that our federal
vernment has never committed itself
an effective international tourism pro-

motion and marketing campaign. The
\$14 million budget of the U.S. Travel &
Tourism Administration ranks no better
than 45th among the nations of the
world in per capita terms and 19th in
total spending terms.

In this global competition among na-
tions—where countries are battling for
tourist trade—we are losing by default.
An adequately funded program to pro-
mote the U.S. as a destination for inter-
national visitors would be an exception-
ally cost-effective investment that would
pay significant dividends for our balance
of trade.

Preston Robert Tisch
Chairman
Travel & Tourism Government
Affairs Council
Washington

Closing the trade gap depends on the
priority we give to aggressively pen-
etrating and developing creative links
with foreign markets. Undoubtedly, in-
ternational efforts are inherently more
frustrating, more risky, and more time-
consuming than most domestic market
activities. And the payoff frequently will
come much later. But the rewards can
be extremely worthwhile.

It's time for America's manufacturers
to knock on a million foreign doors with

open minds, solid products, and creative
thinking. The mechanisms and incentives
for U.S. exports are well in place. It's
long past time to put our goodwill and
our fine words into full gear.

Seth D. Eisenberg
International Vice-President
U.S. Trading Corp.
Tel Aviv

The trend you report in "The little
guys are making it big overseas"
merits attention. However, in describing
the range of support services available
to these companies you failed to observe
that U.S. commercial banks are deter-
minedly ignoring the market sector,
where the growth in our country is.

Fast-growing small companies are be-
ing very poorly served by the banking
community, which, in a supposed "flight
to quality," is making its credit-support
decisions on conservative balance-sheet
criteria.

In a recent survey, more than 85% of
small companies (those with less than
500 employees) reported that they were
obliged to finance their export and for-
eign operations from internal resources.
This inevitably slows down their growth.
Many successful companies are unable
to finance the export sales that their
entrepreneurship, their product technol-



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There's a leather-wrapped steering wheel with a built-in control panel. Radio, air and heat are at y-



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e your dealer for terms of this
ited warranty.

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Readers Report

...y, and their market reputation are generating.

U.S. banks have also deserted the export finance business. Many of their best employees now work for the foreign banks who are expanding rapidly to occupy the empty ground. Others have taken a more innovative course by putting financial muscle behind the potential of successful entrepreneurs.

Too much of today's export assistance really advice from the sidelines that adds to overwhelm the novice exporter with information requiring mastery of a new vocabulary. There is a long way to go before novice exporters get all the financial support they need, even though they are the ones who will dent the deficit anybody can.

Michael T. Schlegel
Managing Director
Trading Alliance Corp.
New York

APOLLO FIRMLY IN ORBIT?

Our recent article "Can Apollo stop hurtling toward earth?" (Information Processing, Feb. 27) questioned the commitment of Apollo's board of direc-

tors to the company's CEO, Tom Vanderslice. As a member of Apollo's board of directors, I can state that Apollo's board is not recruiting a replacement for Tom Vanderslice.

As Director John McKinley was accurately quoted in your article, Tom has the full support and confidence of the Apollo board. This was more than amply demonstrated by our extension of his contract for three more years.

William R. Smart
Member, Board of Directors
Apollo Computer Inc.
Boston

Your feature was regrettably ambiguous regarding Mentor Graphics' continuing support of Apollo Computer workstations. While it is true that Mentor may choose "to adapt its engineering software" to another workstation, a second workstation will be in addition to our Apollo-based systems. Apollo will not "lose" our business.

A large number of our customers feel that the Apollo workstation is technically superior to systems that are competitive. With more than 17,000 Apollo-based design automation systems installed throughout the world, Mentor antici-

pates a sustained, beneficial, and long-term relationship with Apollo.

Thomas H. Bruggere, Chairman
Mentor Graphics
Beaverton, Ore.

CORRECTION

"Ace" Greenberg Tries To Trade Up" (Finance, Mar. 13) said that in a private placement for Triton Group Ltd., "Bear Stearns hiked its fee from 2 to 3.5 percentage points after Triton had committed itself to the buyout. Triton was furious." The deal involved Continental Graphics, a unit of Triton, not Triton. And, while a Continental manager was initially angry because he had expected Michael Tennenbaum of Bear Stearns to spend more time on the \$247 million deal, Continental and Bear Stearns say the original fee was, in fact, lowered from \$3.5 million to \$3.2 million. Both parties say they are satisfied with the deal. BUSINESS WEEK regrets the errors.

Letters to the Editor should be sent to Readers Report, Business Week, 1221 Avenue of the Americas, New York, N.Y. 10020. Fax: (212) 512-6875, Telex: 12-7960, Intl. 4998204. All letters must include an address and daytime and evening telephone numbers. We reserve the right to edit letters for clarity and space.



With the way some facsimiles make you wait,

MY ENEMY, MY SELF

By Yoram Binur
Doubleday • 215pp • \$18.95

PALESTINIAN LIKE ME: AN ISRAELI'S AWAKENING

Among the more troubling aspects of Israel's occupation of the West Bank and Gaza Strip is the scant contact most Israelis have with the 1.6 million Palestinians living under Israeli military rule. The bulk of the Israeli population lives along the balmy coastal plain—a world away from the Arab towns and squalid refugee camps of the disputed territories. For years what little exposure there was came mostly from the thousands of Arab men who ventured into Israel as day workers. Starved for employment in their own areas, they formed a huge pool of cheap labor for menial jobs. Arabs came to be seen as a subservient population, easily exploited and denied basic rights.

At least until last year, the economic benefits of the occupation outweighed the political costs, which could be argued

away on grounds of national security. The human considerations were all but ignored, largely because most Israelis have little sense of the Palestinian experience. Such ignorance—which also pervades the Palestinian view of Israelis—allowed the occupation to continue unchallenged until the Arab population rose up in what has come to be known as the *intifada*, now in its 16th month.

A year before it began, Yoram Binur, an Israeli journalist who had covered the West Bank for several years, decided the way to better understand Palestinians was to become one. Adopting Arab garb and manners, using his fluent Arabic and knowledge of Palestinian customs, he posed for six months as a day laborer in Israel and wandered the refugee camps of Gaza and the West Bank.

The resulting book is important as a

firsthand document of the abuses he saw inflicted on Palestinians by Israelis. That it is written by an Israeli Jew as “warning to my country” gives it added weight as a plea for understanding between the two sides. Binur depicts a society veering close to apartheid. While the status of Arabs in the disputed territories is not comparable to that of blacks in South Africa, it is arguably worse than that of blacks in the segregated American South of the early 1960s.

Posing as Fat’hi, a “son of the camps,” Binur undergoes a catalog of humiliation: He takes on kitchen work in Tel Aviv, earning \$10 for a grueling 10-hour day. Forbidden to stay overnight in Israel, he sleeps illegally on the floor of the rat-infested storeroom. At a series of jobs in restaurants and garages, Binur encounters degradation and racial slurs. One employer suggests he adopt a Jewish name, which would be easier for the employer to pronounce. Another refers to him as “my Arab,” telling friends “With a little improvement, he could be a Jew.” He soon comprehends his standing: “I was invisible, a nonentity.”

The psychological pressures are constant, and physical punishment is always a threat, especially during the dehuman-



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ing ID checks that are a
ray of life for Arabs in
the disputed territories.
Binur is beaten by police
just for being an Arab in
the same area as a group
of Israeli demonstrators.
He lends irony to the
event by recounting his
military service in the
West Bank a decade ear-
lier. As an army officer he
supervised systematic vio-
lence, including beatings,
to terrorize the town of
Ramallah into compliance.
For his successes, Binur
rites, he was made a
judge in the military court
there. Barely out of his
teens, with only a high
school education, he
passed judgment and pris-
on sentences on an entire
population.

Binur is brutally frank
detailing the discrimination Palestin-
ians face. Throughout his masquerade,
however, his dedication to his pose often
alters. Although carrying Arab identifi-
cation, he hangs on to his Israeli ID.
Knowing it to police keeps him out of jail
several times, sparing him the most har-



ISRAELI REPORTER BINUR DONNED ARAB GARB AND POSED AS A DAY LABORER



rowing—and all too familiar—aspect of
a Palestinian's existence. And whenever
he tires of life as an Arab, he abandons
the ruse for several days of comfort in a
Tel Aviv apartment.

In his most irresponsible act, he adds
to poisoned Arab-Jewish relations. At a

kibbutz where he has
stayed briefly as a Pales-
tinian volunteer—improb-
able to begin with—sever-
al thefts occur. As the
only Arab around, he is
suspect. Rather than
prove his innocence,
Binur, tired of the work
and bored with kibbutz
life, vanishes. The kib-
butzniks—among the
more liberal Israelis—are
left to conclude that he is
guilty. Binur has rein-
forced the stereotype that
Arabs can't be trusted.

This cavalier ap-
proach—and a reluctance
to go beyond superficial
reactions and analyze the
fear, hatred, and preju-
dices that stand in the
way of peace—mar an
otherwise worthwhile en-
deavor. Binur writes that

he intended to hold a mirror up to Israeli
society. The reflection would have been
much more revealing if he had looked
deeper.

BY JOHN TARPEY

*Tarpey, who reported for BW from Jordan,
now lives in Pakistan.*

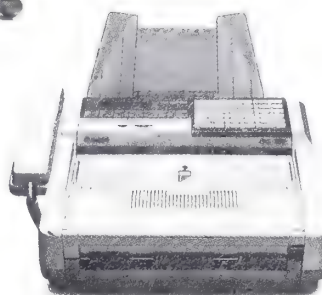


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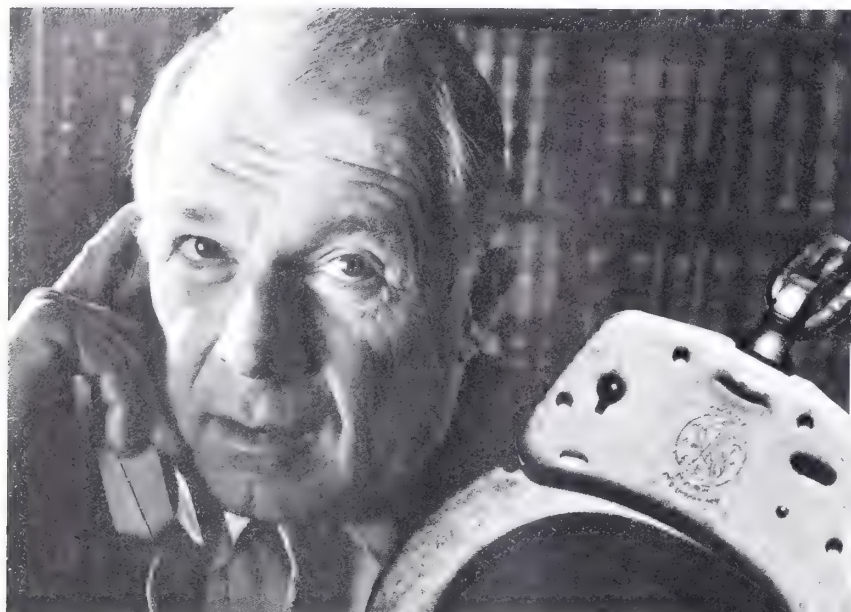


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F. Lee Bailey

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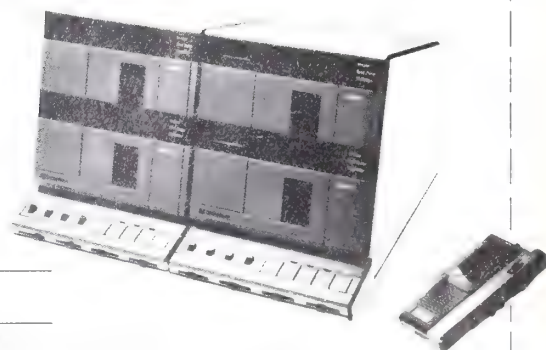
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THE LABOR MARKET IS A LOT LOOSER THAN IT LOOKS

BY ROBERT KUTTNER



The official jobless figures are at a 15-year low. But unemployment is increasingly hidden in the economy—and that's why wages aren't about to push up inflation

The Federal Reserve Board seems convinced that accelerating inflation makes necessary a policy of tighter money and higher interest rates. Yet a closer look at the sources of inflation calls into question the wisdom of this strategy. Conventionally, the economy overheats when labor markets are tight. Wages, however, have been lagging behind inflation for more than two years. In the past two quarters of 1988 wages actually decelerated. The main sources of increased labor costs to industry were higher health insurance premiums and social insurance taxes—neither one the result of feverish economic activity and neither cured by tight money.

The February unemployment rate, 5.1%, the lowest in 15 years, set off new calls for the Fed to apply the brakes. However, even with that decline, average weekly earnings actually dropped by \$1.91, to \$327.22. Moreover, almost all of the drop in unemployment occurred among workers aged 16 to 24 years old. The decline was also disproportionately concentrated among Hispanics, whose unemployment rate dropped by 1.6 points, to 6.8%.

All of this remains consistent with growing evidence that the official unemployment rate increasingly understates the actual amount of slack in labor markets. The Bureau of Labor Statistics' tally of involuntary part-time workers and "discouraged" workers who are no longer in the measured labor force has risen dramatically in recent years. The labor-backed National Committee for Full Employment periodically issues a "real unemployment rate," which adds the discouraged and involuntary part-time workers to the official BLS rate.

The gap between the official rate and the alternative rate has grown steadily wider in each recent business cycle. In 1973 the official rate of unemployment was 4.9%, and the alternative rate was 8.2%; in 1979 the two rates were 5.8% and 9.7%, respectively. For 1988, even as the official BLS rate dropped to 5.5%, the unofficial rate rose to 10.3%. The number of discouraged workers rose from 6.1 million in 1979 to 7.4 million in 1987. During the same period, the number of involuntary part-time workers rose by more than 2 million, to 5.1 million.

WEAKER UNIONS? In the terminology of labor economists, the fraction of jobs that are part of the "secondary labor market"—typically, jobs with less security and lower wages and fringe benefits—has increased relative to those in the primary labor market. Temporary employees now number over 1.2 million workers, many of whom would prefer the wages, benefits, and job security of permanent employment. The number of

such temporary workers has nearly doubled since 1979. The steady decline in the fraction of unionized workers and the diminished ability of unions to bargain for higher wages is also part of this pattern.

All of this goes a long way to explain why the current 5.1% unemployment rate is not generating inflationary pressures of the classical variety. The BLS publishes a number of alternative indices of joblessness, but it has resisted altering its main measures in order to preserve its ability to make comparison over time. However, the greater prevalence of such phenomena as temporary part-time, and discouraged worker, makes such comparisons less meaningful than they seem.

EXTREME CASES. There are two implications of these trends for public policy. First, the Fed should think twice before it applies the monetary brakes on the standard assumption that 5.1% unemployment is inflationary. The Phillips Curve—the alleged trade-off between unemployment and inflation—has a more respectable pedigree than the upstart Laffer Curve, which compares tax rates with tax collections. But like the Laffer Curve, it turns out to be valid only at the extremes. An unemployment rate of 1% would undoubtedly be inflationary, just as 15% unemployment would nicely damp down prices. But in the middle ranges where we live most of the time, there is no simple correlation between shifts in inflation and shifts in employment. Much of the recent jump in inflation reflects the cheap dollar, not inflationary hikes in wages. And much of the underemployment in today's economy is hidden from view. When a discouraged worker or a mother or a part-time worker returns to the full-time labor force, that does not depress the measured unemployment rate or put upward pressure on wages.

The other policy implication is that we should pay more attention to social and competitive aspects of the burgeoning force of contingent workers. Having a reserve of relatively low-wage, part-time workers may help industry lower labor costs in the short run, but it is not necessarily good for America, either as a middle-class society or as an economy that hopes to compete in world markets on the basis of its labor skills. Somehow America needs to generate more good jobs that justify good wages through high productivity—and fewer jobs whose low productivity justifies mediocre wages. In this respect, the news that labor markets are really fairly slack and wages stagnant may be good news for industry, but it is not good news for society.

ROBERT KUTTNER IS ECONOMICS CORRESPONDENT FOR THE NEW REPUBLIC AND AUTHOR OF THE LIFE OF THE PARTY

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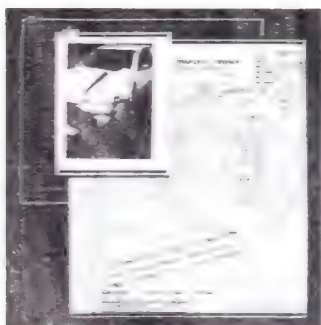


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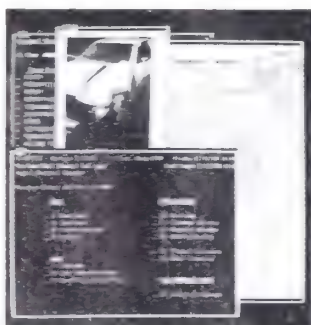
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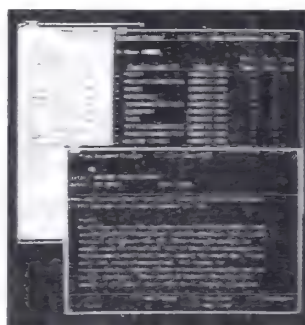
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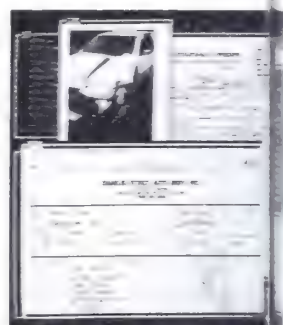
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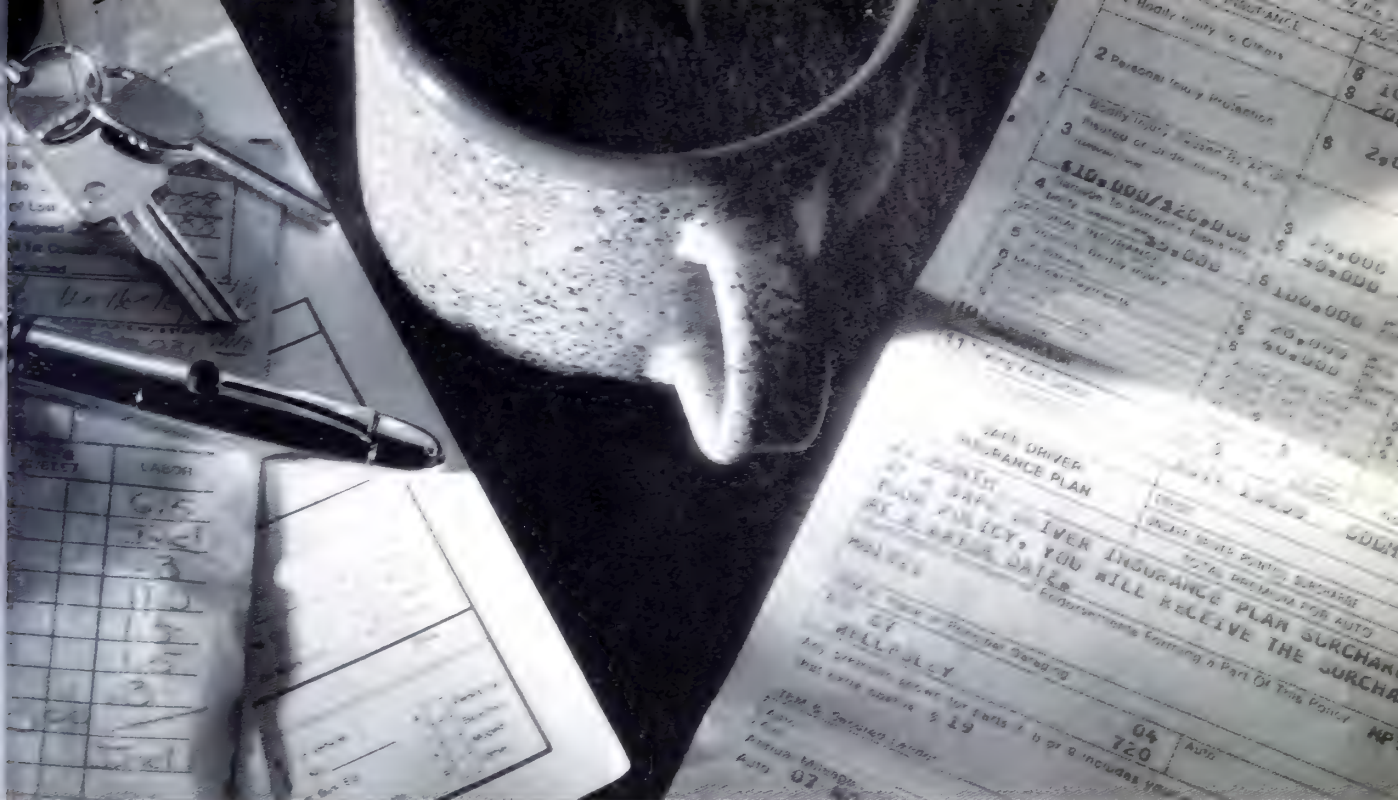
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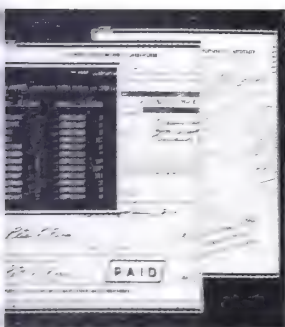
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BY DONALDSON, LUFKIN & JENRETTE

ARE U.S. COMPANIES DANGEROUSLY ADDICTED TO FOREIGN EQUIPMENT?

In the eyes of many economists, relatively strong capital spending will continue to bolster the economy's resilience (page 74). Gert von der Linde and Richard Hokenson of Donaldson, Lufkin & Jenrette Securities Corp., however, see a growing problem in the failure of the devalued dollar to curtail capital goods imports while fostering a veritable boom in capital goods exports.

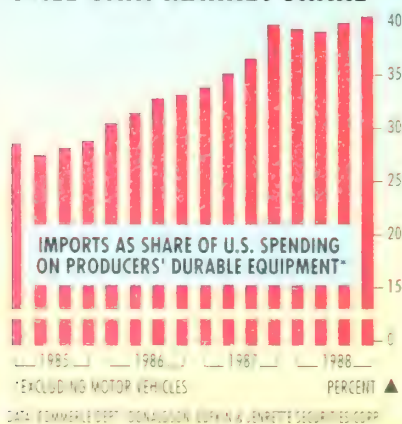
Even those who view the situation more positively are concerned about the

credited with keeping the economy buoyant in recent years, Hokenson and von der Linde estimate that some 69% of the increase in domestic real nonvehicle equipment outlays from yearend 1986 to the third quarter of 1988 was spent on imported goods.

The other side of the coin, of course, is that U.S. capital goods exports have been growing even faster. Sparked by the dollar's sharp descent, they have soared at a 31% annual rate in the past two years. In volume terms, says von der Linde, capital equipment accounted for 43% of total U.S. merchandise exports in the fourth quarter of last year, dwarfing all other export categories. In short, while U.S. manufacturers have become increasingly dependent on foreign-made capital goods (chart), U.S. capital goods makers have become increasingly dependent on sales overseas.

Levine believes that this apparent anomaly will disappear in the years ahead, and that capital goods imports have simply been slower in reacting to the dollar's decline than capital goods exports. But von der Linde and Hokenson are more concerned with the near-term reality of the manufacturing sector's growing dependency on exports. "If foreign demand for U.S. capital goods were to drop substantially," they warn, "we could be facing a sharp slowdown or something worse."

CAPITAL GOODS: FOREIGNERS STILL GAIN MARKET SHARE



apparent anomaly. Economist David Levine of Sanford C. Bernstein & Co. concedes that equipment imports are "a major stumbling block" to progress on the trade front. The conventional wisdom is that the persistent trade gap reflects Americans' insatiable appetite for consumer goods. Yet, as Levine points out, "capital goods are the only type of imported good that has continued to grow robustly in recent years."

From the third quarter of 1986 to the fourth quarter of 1988, for example, capital goods imports (excluding vehicles) rose at a 19.4% annual rate, compared with an average 18.2% rate in the prior six years. By contrast, consumer goods imports, which increased at a 13.4% rate in the earlier period, have been growing at only a modest 2.9% annual pace since then. Indeed, capital equipment imports have accounted for more than 75% of the increase in the nonoil, nonfood import bill over the past nine quarters.

They also have absorbed much of the recent rise in investment expenditures. While capital spending is commonly

THE SOCIAL SECURITY SURPLUS IS PARTLY AN ACCOUNTING ILLUSION

In recent years some bond-market observers have gazed approvingly at the huge projected annual surpluses of the Social Security trust funds. Interest rates, they conclude, must inevitably decline as such huge sums become available to meet the government's needs.

Economist Douglas Lee of Washington Analysis Corp. notes, however, that the Social Security system will have far less cash available for government borrowing than its projected official surpluses suggest. Instead of a projected \$72 billion surplus this fiscal year, rising to \$127 billion in fiscal 1994, he says, the actual cash surpluses of the Old Age, Survivors, & Disability Insurance (OASDI) and Health Insurance (HI) trust funds "will rise from \$44 billion this year to only \$55 billion in fiscal 1994."

The difference between the official and cash surpluses, explains Lee, "is due to the money that is credited to the trust funds as payroll taxes for government employees and interest from past Treasury borrowings from the funds."

Though such interagency payments are essentially bookkeeping entries, the add mightily to the officially reported Social Security surpluses. But the true cash surpluses of the trust funds, which are the difference between cash revenues and outlays, are far smaller.

To be sure, because government payments to the trust funds are counted as outlays in calculating the non-Social Security federal deficit, they overstate the government's actual borrowing needs. But Lee's point is that looking at the official federal deficit and trust fund surpluses obscures the real issue, which is the point at which the system's payments to beneficiaries start to exceed its cash revenues. For the HI trust fund, he says, that will happen in 1995, and for the system as a whole it will happen around 2015. At that point, Social Security will have to start cashing in its government IOUs to pay benefits, even though the OASDI trust fund will still be comfortably in the black.

AN AFFLUENT MIDDLE AGE AWAITS THE BABY BOOMERS

America's most affluent age group is about to experience a population explosion, reports the Census Bureau. As the first baby boomers start turning 45 in 1991, the number of households headed by someone aged 45 to 54 will jump by 51%, to 21.6 million, from 1990 to 2000. That compares with household growth of 14%, or 1.8 million, for the same age category in the 1980s. Recent surveys indicate that members of this young middle-aged group, who are in their peak earning years, enjoy a median income running 43% higher than the average median income of all households.

TOKYO'S TAX CHANGES FLUSH OUT STOCK SPECULATORS

Blame some of the recent selling pressure in the Tokyo stock market on Japan's decision to start taxing capital gains on Apr. 1, advises Brian S. Wesbury of Chicago's Stotler Economics. Under the new law, taxpayers will have the option of paying a tax equal either to 1% of the proceeds of a stock sale or 20% of their capital gain. That means the tax bite declines sharply as the size of a gain exceeds 5%—"a feature that discourages short-term speculation and has provided speculators with an incentive to take profits by April."

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MORE PEOPLE ARE BUSY WORKING— BUT THEY'RE NOT SO BUSY SPENDING

The labor markets are still calling the tune for this economic expansion. February's 15-year low in the unemployment rate will keep consumer confidence high. That, plus robust job gains in January and February, has set up a firm foundation for consumer spending. And that should mean clear sailing for the economy through spring.

However, a couple of storm clouds are gathering. The strength in the labor markets also highlights the economy's vulnerability to inflation—and the Federal Reserve Board's intention to cool off demand with higher interest rates. Consumer demand for cars and other durable goods has been weak recently, but it's not clear if that is the result of Fed tightening or just a temporary lull.

Consumers will not be contributing as much to economic growth this quarter as they did last quarter, when real consumer spending, adjusted for changing prices, rose at a 3.5% annual rate. But that doesn't necessarily mean that consumers are locking up their pocketbooks or cutting up their charge cards.

That's because the big job gains signal continued strength in incomes. Aftertax income grew faster than spending in the fourth quarter, and it's on track to do the same in the current quarter. That suggests any first-quarter slowdown in consumer spending isn't likely to last.

Another cloud is the sharp slowdown in export growth. That may be responsible for some of the softer-reading readings that have been cropping up in manufacturing. Export growth was a big part of the factory sector's vigor last year. The export slowdown puts added pressure on domestic demand to keep industry humming—just at the time when rising interest rates threaten slower growth there as well.

FEWER IMPORTS SHRINK THE TRADE GAP

The merchandise trade deficit in January narrowed to \$9.5 billion from \$11 billion in December. Exports dropped 4.3%, to \$27.8 billion. The drop emphasizes the slowdown in export growth since mid-1988. January exports stood 13.5% above their year-ago levels, but last year at this time growth exceeded 33% (chart).

An 11.4% plunge in capital-goods exports caused most of the drop. Such items are extremely sensitive to changes in the dollar, and the strengthening of the U.S. currency in the middle of 1988 probably weakened the

price competitiveness of those goods in foreign markets.

Imports in January fell even faster than exports, however, and that accounted for the narrower trade gap. Imports, which are now reported excluding the cost of freight and insurance, declined 6.9%, to \$37.3 billion. The early-year malaise in consumer spending showed up in huge drops in imports of cars and other consumer goods.

WEATHER DISTORTED BUYING PATTERNS

Some of that consumer softness was probably weather-related. As expected, many of the February economic data look weak. They're distorted that way because the January numbers were overstated by the effects of the month's unusually mild weather. An average of the two months' numbers gives a more accurate picture of how the economy is shaping up.

That's particularly true for retail sales. They looked much weaker in February than analysts had expected, falling 0.4%, to \$138.2 billion. Sales of credit-sensitive durable goods have been especially weak recently (chart). But the February declines resulted chiefly from the effects of weather and from slumping car sales.

Car sales have been lackluster since December. That month, unit sales of domestically made cars jumped to a strong 8.4 million annual rate. In January and February the annual pace fell off to 7 million and declined further to a meager 6.2 million in early March. But if history is any guide, Detroit's newest round of cut-rate financing deals, with loans going for as little as 4.9%, will give sales a boost in the weeks to come.

Excluding autos, retail sales in February dipped 0.1%. But the weakness there was exaggerated. Nonauto sales in January were exceptionally strong, up 1.4%, reflecting the month's unusually brisk shopping in areas affected by the mild weather. February buying looked meek only because January's was so high.

For example, sales of housing-related items, such as building materials and furniture, were very strong in January but posted declines in February. January sales of all nonauto hardgoods rose 1.6%, but February purchases dropped 0.8%. Sales of nondurable goods showed the same up-and-down pattern, particularly at department stores.

Car sales will be the biggest drag on first-quarter consumer spending, but sales other than autos look sol-



Business Outlook

id. The hefty January performance means that nonauto retail sales began the period on a strong note. For the first two months of the quarter they are 6% above their fourth-quarter average. That's a sign that consumer spending is still fundamentally sound.

Consumers haven't become any more cautious about using credit—despite Fed tightening during the past 11 months. Through January they were still adding heavily to debt loads. Consumer installment credit expanded by \$4.4 billion in January to \$670.6 billion, a shade more than the \$4.3 billion added in December.

Credit growth has slowed a bit in recent months, but that reflects only the softness in car sales. Consumers aren't likely to reduce their credit use as long as robust labor markets are generating incomes and optimism.

PAY HIKES WILL PUT PRESSURE ON PRICES

The labor markets are also generating fears of inflation. February's drop in the unemployment rate to 5.1% from 5.4% in January made that plain. But the labor markets probably aren't that tight—not yet, anyway. The decline was concentrated among teenagers and caused by people leaving the labor pool. That trend could reverse itself in March, pushing the jobless rate back up.

But that doesn't mean the pressure is off the labor markets. Nonfarm payrolls grew by an additional 289,000 jobs in February. That's a healthy increase, especially following the 415,000-job surge in January.

In fact, any weakness in the February report probably reflected January's robust performance stealing some strength from later months. On average, job growth so far in this quarter stands at 352,000 per month—far above the 264,000 averaged in the last half of 1988.

In February, job gains were not widespread. Only 57.3% of the industries surveyed added workers, down from 64.8% in January. And all of the gains were in services, boasting 321,000 new hires. Gains were strongest in retail trade and business and health services.

Jobs in the goods-producing sector of the economy shrank by 32,000 in February. Construction jobs fell by 22,000 last month, following a 105,000 jump in January when unseasonably warm weather boosted building.

Factory employment also declined last month, by 8,000 workers, with large drops in autos, food processing, and lumber. But factory jobs had surged by 53,000 in January—pushing manufacturing employment to its highest in more than seven years. And both the workweek and overtime in February remained high. That means factories are likely to add more workers in coming months.

But with workers getting scarcer, upward pressure on wages is getting greater. Although hourly pay in the private nonfarm sector was up only 0.1% in February, previous pay boosts have been much stronger. Over the past 12 months the hourly wage has grown by 4.2%—the biggest yearly gain in almost five years.

Wage growth in services is leading the pack. Hourly earnings for workers in private service-producing industries have increased by 4.6% in the past year. By contrast, manufacturing wages have risen just 3.2% (chart). And earnings in both sectors are accelerating.

Further wage hikes lie ahead. Congress is moving toward legislation raising the minimum wage from its current \$3.35 an hour. That will bump up all wages at the lower end of the pay scale. And the lack of many skilled workers, such as nurses and engineers, will prompt business to bid up salaries at the high end.

With unions showing fresh interest in wage demands, inflationary pressures in coming months will shift from demand-pull to cost-push, as higher costs of labor and raw materials lead to higher prices.

WHERE WAGES ARE RISING FASTEST



THE WEEK AHEAD

CONSUMER PRICE INDEX

Tuesday, Mar. 21, 8:30 a.m.

Most economists expect that consumer prices increased by 0.5% in February, following a 0.6% jump in January. Higher energy prices accounted for much of last month's increase, but other price pressures are building, too. In January the "core" rate of inflation—prices excluding food and energy—rose 0.5%.

FEDERAL BUDGET

Tuesday, Mar. 21, 2 p.m.

The federal government will probably post a \$25 billion deficit for February, not much different from the \$24 billion recorded a year earlier. With February's expected budget gap, the federal deficit

so far in fiscal 1989 would total about \$90 billion, the same pace as in 1988, when the budget finished the year \$155 billion in the red.

DURABLE GOODS ORDERS

Wednesday, Mar. 22, 9:30 a.m.

New durable-goods orders likely fell by 1% in February. Orders dropped 2.7% in January, but that followed a 7.4% surge in December. The backlog of hardgoods orders remains strong, however. Unfilled orders, which rose 1% in January, are 11.8% above their year-ago levels.

PERSONAL INCOME

Friday, Mar. 24, 10 a.m.

The consensus is that personal income in February rose a moderate 0.5%. Farm

subsidy payments and another large increase in interest income will boost overall earnings. Wage and salary growth was probably weak, as indicated by the drop in weekly earnings in February. In January personal income rose 1.8%.

CONSUMER SPENDING

Friday, Mar. 24, 10 a.m.

Consumer spending probably edged up just 0.2% in February. That's suggested by the declines in new-car sales, when measured in dollar terms, and in other nonauto retail sales. The expected weak spending in February will help to keep the savings rate high. But when coupled with the slight 0.1% rise in January, the number also indicates some weakening in first-quarter consumer spending.

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TEXAS AIR: EMPIRE IN JEOPARDY

AS LORENZO FIGHTS TO HANG ON AT EASTERN, CONTINENTAL IS IN A DOWN DRAFT

The grudge match between Texas Air Corp. Chairman Frank Lorenzo and the striking unions of Eastern Air Lines Inc. only gets nastier. As union strategists gird for a titanic struggle over Eastern's fate in bankruptcy court, they're making a fresh advance on Continental Airlines Inc., the heart of Lorenzo's empire.

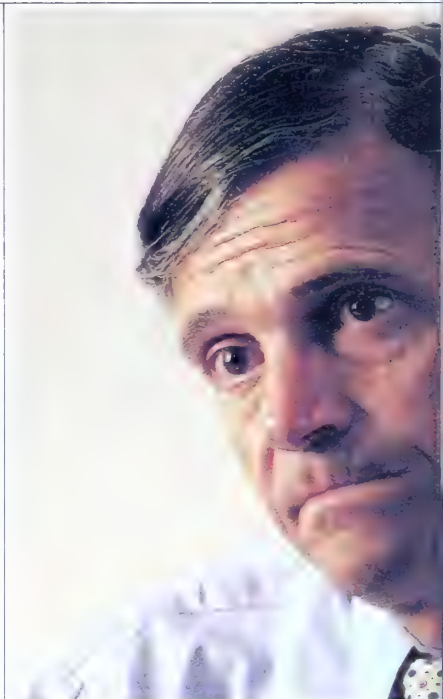
Striking machinists are picketing Continental at its critical Houston and Newark hubs. And Eastern's pilots, claiming that Lorenzo pillaged Eastern to prop up Continental, are trying to drag Continental into bankruptcy court. Perhaps most threatening of all, the unions hope to capitalize on the hurt Eastern caused its customers, who were stranded for days with worthless tickets. Union leaders may hand Continental's advanced-ticket buyers leaflets that ask: "Are you sure you'll get your money back?"

More trouble at Continental is the last thing Lorenzo needs. With Eastern in Chapter 11, Texas Air simply must make money at Continental. Many analysts

confidently predicted that it would bounce back for good last summer. Instead, Continental kept losing money, furthering losses that have totaled \$574 million since January, 1987. Between the red ink and Eastern's intractable woes, Texas Air has plunged from a brief role as the non-Communist world's biggest carrier to a profitless third place behind American Airlines Inc. and United Airlines Inc. While other airlines posted fat profits last year, Texas Air's losses came to a stunning \$718.6 million.

Few foresaw any of this just two years ago, when Texas Air shares soared to \$51.50 (chart). Nonunion Continental was a showcase, the crowning achievement of Lorenzo's remarkable career. Eastern, which he had picked up with a lowball bid just months before, only burnished that reputation.

SOLE CHALLENGE. Lorenzo made his way with a peculiarly lonely brand of grit and determination, from an upbringing in Queens, N.Y., to a first job as a financial analyst at Trans World Airlines.



FRANK LORENZO'S TURBULENT CAREER



1972-79

Through his investment firm, Jet Capital, Lorenzo buys control of tiny Texas International for \$1.5 million, using "peanut fares"

to fill his planes. TI loses to Pan Am in a 1978 bidding war for National Airlines, but makes \$40 million on its National stock.

1980

Lorenzo creates non-union New York Air and forms Texas Air as a holding company.

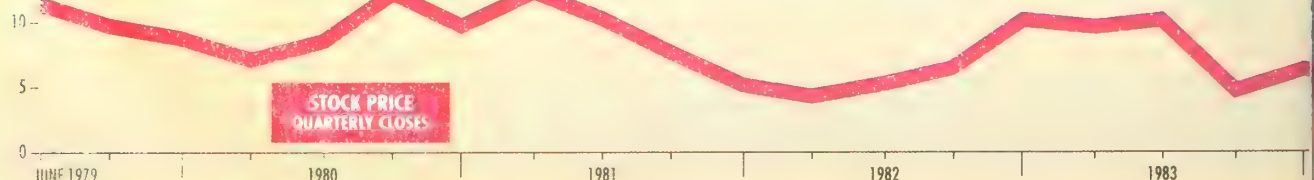
1982

Texas Air buys Continental Airlines for \$154 million.



1983

Continental files Chapter 11, proving a walkout by unionized workers. Lorenzo replaces with nonunion workers at much lower wages.



In 1969 he put together a \$35,000 grubstake to form an airline consulting and leasing firm and steadily built it into the sole startup to challenge the supremacy of such established carriers as American and United. Many now wonder whether Lorenzo learned enough about day-to-day operations in his 17 years of running an airline to support his truly visionary strategy. Even loyalists acknowledge that Continental's operations have frequently been ill-prepared and poorly executed. Lorenzo

would not comment for this story.

Much of the blame for the carrier's troubles can be laid to its purchases of People Express/Frontier Airlines and Eastern in 1986. That put Texas Air on top, but merging the operations became a nightmare. Some People Express Inc. pilots were so angered by their treatment under Lorenzo that they refused to talk to some coworkers in the cockpit.

While other airlines made fat profits last year, Texas Air lost \$718 million

Another typical blunder: a marketing plan, which went into effect early last year, that offered unnecessarily cheap fares—with red ink the result. "At first we all assumed Lorenzo had a plan," says a former Eastern executive. "After a year we realized there was no plan."

What's more, Lorenzo's style of management, as much as its substance, has also added to Texas Air's woes. No one doubts his intelligence. Yet to a degree unmatched in any major labor-management confrontation of recent years, Lorenzo the man has been the central issue.

Given the depth of Continental's problems and Lorenzo's own demanding personality, it's no surprise that Continental has labored under five bosses in as many years. The latest: D. Joseph Corr, the ex-president of Carl C. Icahn's TWA. Corr is praised for slashing TWA's costs and sending operating profit up sharply.

At Continental since January, Corr

has been a blur of motion. When he first laid eyes on Continental's 1989 draft budget, says one insider, he promptly declared it unacceptable. The reason: a forecast of more red ink. Working for nearly nine weeks straight, Corr immersed himself in the books. One Continental executive says Corr has created "an overall sense of emergency."

PRECIOUS PICKUP. That's the very least it'll take for Corr to get Continental out of the tailspin that has drained parent Texas Air and sibling Eastern of \$555 million in cash since January, 1987. In the short term, Continental will profit from the Eastern strike: Continental picked up the lucrative New York-to-Miami routes that Eastern can't service. And Continental's planes have been carrying heavier loads in March—a switch from the year's first two months, when passenger lists were a lot shorter than in 1988. Continental managers, who had predicted losses for both the first and second quarters, now say the carrier may break even by June.

That would be a major achievement. But to build profits for the long term, Continental must pull off a far trickier stunt: luring business travelers, who pay the highest fares. Until December, the airline positioned itself as the low-fare carrier, more likely to shuttle tourists than executives—a no-frills marketing program that alienated prime clients.

Continental has miles to go before it is truly appealing to business travelers. Corr is counting on improved service and is likely to rely on a joint venture formed in October with Scandinavian Airlines System. SAS is supposed to form a quality-training institute for Contin-

's embattled Hank Borman say to Lorenzo, Texas Air agrees to term. It takes

Continental out of Chapter 11, then strikes a deal for Donald Burr's failing People Express-Frontier.



ALL-TIME HIGH:
\$1 1/2 (FEB. 1987)



1988

As Eastern battles with the machinists' union, the government launches safety investigations of Continental as well as Eastern. Year-end losses at Texas Air exceed \$718 million.

1989

After 15 months of fruitless talks, machinists at Eastern strike. Eastern files for Chapter 11, with Continental still losing money.

1985

1986

1987

1988

MAR. 14, 1989

DATA: BRIDGE INFORMATION SYSTEMS INC.

tal. The venture also may benefit Continental by linking it to SAS's international routes. But the institute won't be up and running until the fall, and links to SAS routes aren't likely to pay off anytime soon.

Corr must also find a way to exploit Continental's cost advantage. Nonunion Continental's average costs rank about 18% below the industry average. But Corr's predecessors, plagued by the problems of digesting acquisitions, never succeeded in using that edge to grab—and keep—market share. Now, Delta, American, and United, with strong balance sheets and clean reputations, are on their way to industry domination.

That all sounds like enough to keep one experienced airline man busy. Yet Corr—and Lorenzo—must also contend with the perils posed by Eastern's bankruptcy. If the bankruptcy court forces Texas Air to cover Eastern's unfunded pension liabilities, estimated at up to \$750 million, or make good on the guarantees it has made on some Eastern interest payments, the parent would have very little to spare for Continental. Continental executives insist they won't need cash in 1989. But if they're wrong, Continental's estimated \$140 million in the till could be nearly depleted.

That's why Lorenzo's struggle in bankruptcy court is critical not just to Eastern but to the survival of Texas Air. Few know what Lorenzo's bankruptcy strategy is. He has denied that he wants to liquidate Eastern, but one industry source says he's talking with American about a deal to sell Eastern's prized Latin American routes. He also says he wants to keep Eastern, or at least part of it, but according to rival investment bankers, he has authorized Drexel to consider bids for the airline.

RUSHING IN. While Eastern's ultimate fate will be decided in court, its immediate future remains in the hands of the striking Eastern pilots, whom Lorenzo dearly wants to lure back. But the pilots have held firm, and Eastern has been able to put only about 10% of its flights in the air. So losses mount. Given a month, the company might recruit and certify enough new pilots to resume many more flights. But by then, as competitors rush to offer passengers a way to their destinations that avoids picket

lines, the damage could be irreparable.

Nor are the unions simply saying: "We won't work." They're demanding to run things. And they're trying to interest the likes of Icahn in a joint takeover of Eastern. They also hope to wrest control of Eastern from Texas Air in bankruptcy court, a strategy they had devised even before Eastern's attorneys filed for Chapter 11. Eastern's bankruptcy counsel, Harvey R. Miller, believes the court will halt the unions' advance: "This has taken on the dimensions of a holy war," he observes, "and any bankruptcy court will take that into account."

If it is indeed a holy war, to the

organization plan before Lorenzo sell more assets. "You don't reorganize by selling off the good parts," argues Farrell P. Kupersmith, a Touche Ross & Co managing partner and the pilots' financial consultant. The first test will come soon enough: Eastern's \$365 million sale of the Boston-New York-Washington shuttle to Trump Airways, the new carrier formed by New York real estate developer Donald Trump. The new carrier will soon have all the regulatory approvals it needs to begin operations.

MIXED REVIEWS. Meanwhile, creditors and stockholders are worrying and warring over the real value of Eastern if

Lorenzo sells it off whole or in parts. Some who own the stock are optimistic. "You can get pretty easily to a value of \$12 a share for Eastern alone," says Michael Steinhardt, a big Wall Street money manager. "That makes it worthwhile to stick around with the stock." Others, including Michael Salshutz, an L. F. Rothschild & Co bond analyst, are skeptical of Lorenzo's assertion that Eastern is worth \$1 billion even after it pays off its liabilities. Salshutz thinks Eastern's current liquidation value could be well under \$700 million.

Whatever Eastern is worth, its value won't be realized fast. "Everyone starts off with high hopes that a bankruptcy will be done quickly," observe

Donald M. Roberts, an executive vice president at U. S. Trust Co., which functions as a trustee for investors holding \$58 million worth of Eastern bonds. "But I've yet to see one bankruptcy done quickly."

So it is that Frank Lorenzo, visionary airline builder, is zooming toward earth at too steep an angle, way too fast. Only if Joe Corr can get Continental's engine thrusting again—and Lorenzo can pull Eastern out of bankruptcy with his hands still on the controls—will once mighty Texas Air stand a chance to turn the profit that has eluded it for years.

There's little question Lorenzo will work doggedly toward that end. But without more good luck than he might reasonably expect, Frank Lorenzo shouldn't count on reversing the disintegration of the empire he toiled 20 years to build.

By Todd Vogel in Houston and Gail Dolan, George and Pete Engardio in Miami, with Aaron Bernstein in New York

EASTERN: A SWEET DEAL FOR TEXAS AIR

TRANSACTION	WHAT TEXAS AIR GAVE EASTERN	WHAT EASTERN GAVE TEXAS AIR
Texas Air buys Eastern (1986)	\$277 million in cash*	Airline with market value of \$570 million
Eastern sells assets to Texas Air (1987-88)	\$179 million in notes, plus \$102 million in cash	Six Airbus A300s, 11 airport gates, computer reservation and software divisions
Management contracts (1986-88)	Strike contingency preparations, other management services	\$62 million in cash
Notes and guarantees (1987-88)	Guarantee of some Eastern interest payments; notes to Eastern	\$40 million cash deposit; \$64 million in cash
Eastern's estimated liquidation value (1989)	—	\$650 million—\$1 billion

*Eastern paid its own shareholders an additional \$108 million in cash, plus \$230 million in preferred stock, for a total of \$615 million.

DATA: COMPANY REPORTS, L. F. ROTHSCHILD, TEXAS AIR ESTIMATES

unions, Lorenzo is the infidel. On Mar. 14 the pilots' union asked the court to remove Lorenzo as Eastern's chairman. Their reasoning: Lorenzo milked it for cash, leaving behind a shriveled sack of money-losing operations. Eastern attorney Miller responds that he's tired of the asset-stripping charges, which he says are false, and on Mar. 13 he asked for an independent auditor to examine the asset transfers. But a look at the deals seems to show that Texas Air wound up a winner at Eastern's expense (table).

Union leaders also want to convince the court that Eastern must file a re-

'This has taken on the dimensions of a holy war, and any bankruptcy court will take that into account'

THE WINGS OF MAN WEREN'T BROKEN OVERNIGHT

Is venerable Eastern Air Lines Inc. a victim of deregulation? That's the cry in Washington these days, as legislators, spurred on by Eastern's recent bankruptcy filing, vow to investigate the excesses of the airline industry and protect passengers from predatory pricing by the megacarriers. With Eastern forced to the brink, it seems to many in government that deregulation has brought another once-powerful competitor to its knees.

Yet it would be foolish to blame Eastern's tragedy on deregulation alone. Sure, Eastern was bloodied by the Darwinian struggle that followed the airline industry's deregulation in 1978. But Eastern also has been a financial laggard since the 1960s (chart), often finding itself in the red—quite a trick for a company operating in what was then a regulated oligopoly. In fact, if Eastern's situation is an example of the brutal consequences of deregulation, it's also a telling lesson in how poor management can hurt a company long after the poor managers are gone. **LAVISH PERKS.** Eastern's first big blunder came at the start of the jet age, when Chairman Eddie Rickenbacker, the World War I ace, canceled an order of DC-8s. He figured he could still get by with prop-driven planes. Delta Air Lines Inc. picked up Eastern's order and used the DC-8s to establish supremacy over Eastern.

The managers who followed Rickenbacker's 1963 retirement fared no better. Executives fought each other for power, often adding expensive layers of management in the process and blowing fortunes on lavish perks. The company's strategists entertained grandiose schemes, such as the purchase of a supersonic transport. Even wonder Eastern lost huge sums even when the Civil Aeronautics Board, not market forces, set fares.

Perhaps most important, Eastern's managers failed to fix a fundamental strategic problem at Eastern: The airline was a North-South carrier, dependent on wintertime tourists for profits and forced to compete on the heavily lousy routes between New York and Miami. Pan American World Airways Inc. had a similar weakness, because it

depended on summer transatlantic traffic for its profit. It's no coincidence that Pan Am and Eastern today are the industry's weakest carriers.

Like Pan Am, Eastern kept going, partly because financiers are often willing to invest in a company that can offer attractive assets, such as jets, as collateral. Nevertheless, by 1976 when ex-astronaut Frank Borman became chairman, Eastern was well on its way to disaster. As Raymond E. Neidl, an

by opening a hub in Kansas City.

But Borman made a critical error. His bold, \$1.4 billion investment to rebuild an aging fleet with fuel-efficient Airbus Industrie A300s and Boeing 757s saddled Eastern with more debt than it could handle just as deregulation dawned. And when oil prices crashed, the competitive edge promised by the new fleet disappeared. Deregulation also spawned fresh rivals, like People Express Airlines Inc., that

launched fare wars on most of Eastern's major routes. As losses soared, Borman repeatedly demanded pay cuts from the unions, who grew foolishly cynical about management's dire warnings. Finally, the losses and the rancor between labor and management forced Eastern to accept a lowball bid from Frank Lorenzo.

Lorenzo was Eastern's last hope. Had he cut a deal with the machinists, trading cuts in labor costs of, say, 15%, for stock or other considerations, Eastern would

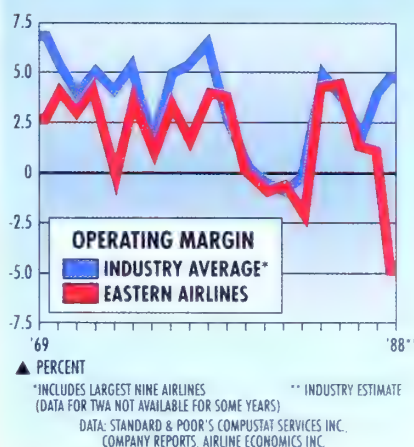
likely be flying toward recovery today. But by 1986 when Lorenzo arrived, both management and labor had long since stopped dealing rationally.

Lorenzo insisted all along that he was a builder, not a union buster. But his tough contract demands and his stockpiling of \$1 billion in cash as strike insurance all seemed transparently designed to precipitate a walkout he might then crush, as he did in 1983 at Continental Airlines Inc. As Lorenzo maneuvered with the unions, Eastern adopted a ruinous policy of downsizing. The result: the strike by 8,500 machinists and 3,800 pilots that will likely cost them their jobs—because when it ends, there will be little left of Eastern.

It didn't have to be this way. Other airlines had Eastern's weaknesses and emerged stronger from deregulation. Delta, for example, was largely a North-South carrier, but it successfully built an East-West network. The airline also had on its side a tradition of quality service, cordial relations with workers, and no-frills management. Years ago, Eastern might have learned a lesson or two from Delta. It's too late now, when the best hope is that Eastern gets a decent burial and more competent airlines take over its routes.



EASTERN TRAILS THE PACK



airline bond analyst who turned down a chance to work for Eastern 10 years ago, recalls: "Eastern was a high-cost, low-yield airline with a lousy service reputation and militant unions."

FARE WARS. Borman's promotion to the chairman's office did hold promise. His earnest, strictly-business approach lowered overhead and persuaded employees to make wage concessions. He also moved to wean Eastern from its dependence on North-South routes



GERSTNER AND SNACKS: HE HAS ALREADY BOOSTED MORALE WITH A WHIRLWIND, FLAG-WAVING TOUR OF RJR NABISCO'S MAJOR U.S. UNITS

LOU GERSTNER IS GIRDING FOR A LONG, HARD CAMPAIGN

He has to pay \$3 billion in interest—and he has to market cigarettes

When Louis V. Gerstner Jr. first entertained the idea of heading RJR Nabisco Inc., the nonsense American Express Co. president raised his strongest reservations early on. In a secret interview at his Greenwich (Conn.) home one Sunday in January, the executive fielded a battery of queries from Kohlberg Kravis Roberts & Co.'s leveraged-buyout king Henry R. Kravis and partner Paul E. Raether. "I was impressed with their questions," Gerstner recalls. "But I told them: 'If you're looking for a liquidator, I'm not your guy. I'm a builder.'"

Talk, of course, can come cheap, especially when it's about the risky future of the \$25 billion leveraged buyout of RJR. But by luring the tough-minded heir apparent to the AmEx throne into the chairman's slot at RJR, KKR strengthens its promise not to dismember the company but to manage it for the long haul. Even RJR insiders, suspicious that KKR intends to break up the company, are heartened that they have a leader who is a proven operator. "I'm believing Henry Kravis that this is a long-term investment," says H. John Greeniaus, chief

executive officer of Nabisco Brands Inc. "Gerstner is no quick-fix artist."

Although Gerstner doesn't take command until Apr. 3, he has already helped boost morale with a whirlwind, flag-waving tour through RJR's major U.S. operations. While he says it's too early to disclose specific plans, he indicates that his first priority is to "settle down" the organization, which was whipsawed by the LBO and, before that, by the unpredictable style of former CEO F. Ross Johnson. Another early decision will be whether to move headquarters from Atlanta to Winston-Salem, N.C., or, as is widely speculated, New York. Gerstner also vows to get the company's asset sales under way. An estimated \$6 billion must be raised to pay off bank notes due in two years.

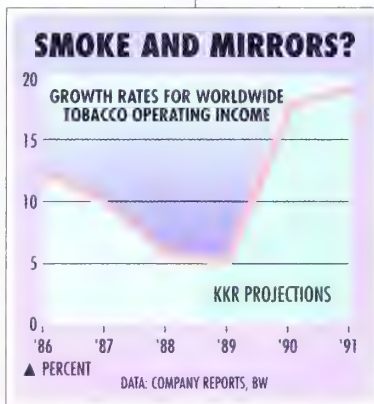
Despite RJR's \$3 billion in annual interest payments and rising rates on its

floating-rate debt, Gerstner says he feels no immediate pressure. "We aren't going to, and we don't have to, fire-sell assets," he asserts. Likeliest candidates for sale include Del Monte, Planters Life Savers, a stake in ESPN, and some of RJR's international food units.

TOBACCO WOES. One of Gerstner's top priorities will be stemming the erosion in the cigarette business, which provides 61% of RJR's \$2.8 billion in annual operating income. In the past year alone, RJR has experienced sharp declines in its share of the domestic cigarette market and, worse, in its profit growth. RJR and its aging Winston and Salem brands keep losing market share to Philip Morris Cos., whose slice of the market last year rose 1.5 share points, to 39.3%, compared with RJR's decline of nearly a point, to 31.7%.

Meanwhile, RJR's growth in tobacco profit is faltering, falling to a 5.6% rate last year from a 9.8% increase in 1987. Gerstner will have to turn that trend around fast if he is to meet the optimistic forecasts KKR made at the time of the buyout (chart). "The biggest business challenge is tobacco," concedes interim RJR Nabisco Chairman J. Paul Sticht.

Worse, the decline in the domestic cigarette



cigarette business is accelerating. And that's during a period when many industry observers think cigarette companies will have to ease up on their aggressive price hikes of the past, which have pushed the average price of a pack of cigarettes up more than 50% in the past five years, to about \$1.35. In addition, tobacco companies already have wrung much of the margin gains possible from plant modernizations and consolidations, many onlookers say. Gerstner's solution? "You increase share," he says. "This company has five of the best-selling brands in the industry, and only five years ago, Philip Morris and RJR were plugging it out toe-to-toe."

ADEPT STRATEGIST. While Gerstner has never faced the unique social and political challenges facing the cigarette industry, he has shown an ability to boost businesses that long ago were branded as mature. When he came to AmEx' Travel Related Services Co. 11 years ago, analysts had low expectations of the company's venerable traveler's check and American Express card businesses (box).

The former McKinsey & Co. finance consultant has proved himself an adept strategist, too. At McKinsey, he was the chief financial architect of the Penn Central bailout. More recently, he helped craft AmEx' spinoff of Fireman's Fund Corp. He reduced AmEx' exposure to the cyclical brokerage and investment banking business by selling 39% of Shearson Lehman Hutton Inc. "RJR needs a guy of this caliber," Sticht says. The key question is disposing of enough assets so you can still build the tobacco and food business back."

Even if he can devise the right strategy and balance his need for capital with the strict requirements of servicing RJR's debt, Gerstner faces the daunting task of rebuilding RJR's culture. "It's been a traumatic six months—not to mention the last two years," says one RJR manager. Can Gerstner recreate the innovative environment he helped establish at AmEx? At the least, he may find it difficult to enlist top managers to RJR's battle-weary ranks. As one former Gerstner associate notes: "No one's running to get into the tobacco industry."

Gerstner says he isn't underestimating the difficulties of managing RJR. The 7-year-old is putting his fast-track career on the line, saying it was the challenge that attracted him to the job. Of course, his five-year compensation package of \$25 million didn't hurt. The money should also console Gerstner for the rings he'll likely have to give up—such as his directorships at the National Cancer Advisory Board and the Memorial Sloan-Kettering Cancer Center.

By Scott Ticer in Winston-Salem, N. C., with Frederic A. Miller in New York

RJR'S GAIN COULD MEAN PAIN FOR AMEX

For a moment, American Express Co. shuddered. After President Louis V. Gerstner Jr.'s surprise resignation was announced on Mar. 13, his colleagues "hit the floor and bounced," Gerstner says. "But then they got right back up again." The smooth publicity machine swung into action. Chairman James D. Robinson III assumed the AmEx presidency. And in a video taped that night and sent to 50,000 employees worldwide, he announced that Aldo Papone would take over Gerstner's duties as CEO of AmEx' crown jewel, American Express Travel Related Services Co., which

boosted AmEx' charge volume at retail stores. Papone, Gerstner's chief operating officer, predicts a smooth transition. AmEx will need one, as it installs a new data base architecture and prepares to set up First Data Resources Inc., its money-making computer services unit, as a separate company.

Papone admits he will miss Gerstner's strategic sense. And AmEx has long-term worries. As its charge volume grows, so do its credit risks: Loss reserves rose 31% last year. And then there are the bank cards, which are fighting for a larger share of business-travel spending. If Amex counters too aggressively, MasterCard International Inc. President Alex W. Hart predicts that banks will stop selling AmEx traveler's checks.

But AmEx is so entrenched that rivals draw no satisfaction from Gerstner's departure. Its traveler's checks, once dismissed as "mature," have doubled in sales over the last decade, to \$24 billion. The resulting \$3.8 billion float not only gives a juicy return but also offsets AmEx' interest-rate risk, says Cooperman. The



CEO ROBINSON: HE ASSUMED THE AMEX PRESIDENCY HIMSELF

earned \$773 million last year—more than three-quarters of AmEx' total. "The king is dead, long live the king," says Edwin M. Cooperman, head of the U. S. card division.

Just the same, Gerstner's abrupt departure opened a hole that will be hard to fill. "Lou was irreplaceable," says Director Henry A. Kissinger. His timing, from AmEx' perspective, is not so hot, either: Robinson is already hunting for a replacement for Robert F. Smith, chairman of the sluggish American Express Bank, who took early retirement on Mar. 1. And Gerstner helped Robinson steady the company's control over its Shearson Lehman Hutton Inc. subsidiary, which has its own share of defections and financial woes.

SMOOTH TRANSITION. Papone, a 56-year-old marketing whiz who joined AmEx after 18 years at R. H. Macy & Co., draws praise for the new Optima card and savvy promotions that sharply

AmEx card faces a paradox: how to grow without jeopardizing its elite image. So far, though, "they've dealt with it very well," says James L. Bailey, chief of Citicorp's U. S. bank cards. "They have a wonderful franchise."

Robinson was stunned by Gerstner's departure. But he welcomes closer contact with executives who may succeed him in the early 1990s as AmEx boss: "For the first time in 12 years as CEO, I get to monkey around," he jokes.

Gerstner once worried aloud that entrepreneurship might fade at AmEx if he left. Now, Gerstner takes pride in leaving AmEx with strong managers. "If I'd left them in the lurch, that would have been very difficult for me," he says. That's no longer a problem. In fact, Gerstner recently told a friend that he had too many smart executives who needed promotions. He solved that problem in a hurry.

By Frederic A. Miller in New York



JOHN KISSICK, DREXEL'S CHIEF FINANCIAL OFFICER, AND
MICHAEL R. MILKEN, DREXEL'S CHIEF EXECUTIVE OFFICER

JUNK BONDS

WITHOUT MILKEN, CAN DREXEL STILL BE DREXEL?

John Kissick has to convince the boardrooms that it can

For much of the past decade, John H. Kissick carried Michael R. Milken's junk-bond gospel to the executive suites of Corporate America. Now the Yale graduate and onetime Navy officer faces the biggest selling job of his career. With Milken all but out at Drexel Burnham Lambert Inc., Kissick must promote the notion that the Milken empire won't crumble without its creator.

Drexel insiders say Kissick, 47, will assume command of the high-yield department when the firm completes a settlement agreement with the Securities & Exchange Commission. That pact will include Milken's dismissal. Kissick is seen both inside and outside Drexel as a strong manager who won't try to build a firm within a firm, as Milken did.

IRON GRIP. Kissick has already spent much of the past year plotting a post-Milken strategy that will rely more than ever on smaller companies and offshore deals. The firm can still pull off a blockbuster, such as raising \$5 billion privately for Kohlberg Kravis Roberts & Co.'s buyout of RJR Nabisco Inc. But the firm wants to focus more of its attention on financings of \$150 million or less. About half the firm's 20 pending deals are in that range, including offerings

for Playtex Apparel Inc. and Zale Corp.

By concentrating on smaller underwritings, Drexel is acknowledging implicitly that its iron grip on the junk market has weakened. "I don't think they've slipped in their competence or ability, but their market ranking has slipped," says Hamilton E. James, a managing director at Donaldson Lufkin & Jenrette Securities Corp. At this time last year, Drexel had already underwritten \$1.2 billion in public junk offerings, 36.5% of the market. But Drexel's total so far this year is only \$533 million. That gives it 14.6% of public issues, well behind Goldman, Sachs & Co. and Merrill Lynch & Co. Its share of the public market should improve as the year progresses, and it's still a major force in private placements.

Drexel's waning market power isn't solely a function of stiffer competition. The firm's legal problems have prompted some of its clients to look elsewhere. After Drexel agreed to plead guilty to manipulating securities of Stone Container Corp., that company took its financing business to First Boston Corp. Kissick admits Drexel's two-year legal struggle has taken its toll. "It hasn't been like getting hit with a sledgeham-

mer," he says, "but more like a little hammer tapping down on us."

Helping Kissick to withstand the blows has been Peter Ackerman, a key Milken aide. Like Milken, the 42-year-old Ackerman has a knack for devising innovative features that make difficult placements easier to sell. "Peter can play an important role in lending his expertise and creativity in a lot of different places," says DLJ's James.

Ackerman, who holds a PhD in law and diplomacy from Tufts University, proved his worth in the RJR deal. He used the lure of RJR stock to persuade holders of RJR notes to convert their holdings to longer-term bonds when they're issued in April. The idea worked so well that the note offering, originally set for \$3 billion, was oversubscribed.

To underline the importance of foreign financings, the firm is expected to put Ackerman in charge of drumming up overseas deals. In January the firm raised \$387 million in Australian-dollar-denominated bonds for John Fairfax Ltd., a troubled Australian magazine and newspaper publisher. To entice U.S. buyers, Ackerman gave them a chance to profit from currency fluctuations.

Drexel is counting on the Fairfax deal to catch the attention of the cadre of expansion-minded financiers in Australia and other Pacific Rim countries, who've been relatively quiet since the 1987 market crash. The firm can count on former Treasury Secretary William E. Simon to help spread the word: He's the one who brought Fairfax and Drexel together.

UNFAZED: But spotting new or expanding markets won't get Drexel very far unless Kissick and Ackerman keep the Milken team—staffers and customers alike—together. Million-dollar salaries help satisfy the hired hands, of course. But there have been some defections among Drexel's stable of longtime investors. Columbia Savings & Loan Assn. for instance, has been throwing more of its business to Drexel's competitors.

Kissick is unfazed. "What's remarkable to me is that we lost so few [staff] people," he says. "Now the challenge is to keep the franchise together." To do that, Kissick has been on the phone constantly to clients, reassuring them that the firm is still strong and imaginative.

Deals such as the RJR coup bolster his pitch. And he can do more selling at the annual Predators' Ball, the Woodstock of the high-yield set. In previous years, Frank Sinatra and Kenny Rogers provided the entertainment while Milken worked the crowd. Drexel won't say who's headlining the April bash. But you can be sure Kissick will be putting on a show of his own.

By Eric Schine in Los Angeles

WHY THE NICKEL-AND-DIMING OVER THE MINIMUM WAGE?

Liberals and conservatives have long engaged in a pitched battle over the minimum wage. Business groups warn of inflation and devastating job losses, especially among black teens, if the wage goes above \$3.35 an hour. Labor argues that the current minimum is too meager to lift families out of poverty. But as a measure to raise it moves through Congress, the fight has degenerated into little more than political theater. The reason: In economic terms, the minimum wage doesn't matter much anymore.

Why not? Because only a small and steadily shrinking proportion of today's work force earns it. Inflation and labor shortages have boosted entry-level wages far above the federal minimum since it last was raised, in 1981. Last year only 3.9 million workers, or 6.5% of hourly wage earners, earned the minimum, down from 15% in 1981 (chart). Even the percentage of workers earning a few notches above the minimum—from \$3.50 to \$4.50 an hour—has dwindled from 21% of hourly workers in 1981 to 13% last year.

The trend shows no sign of letting up. Unemployment fell to 5.1% in February, its lowest rate in more than 15 years. "The competition that's driving up wage rates will make an increase in the minimum wage almost irrelevant," says economist Bernard E. Anderson, managing partner of the Urban Affairs Partnership in Philadelphia.

NONWORKING MODEL. Of course, economic reality rarely stops the bickering on Capitol Hill. Labor and liberals are supporting a measure by Senate Labor & Human Resources Committee Chairman Edward M. Kennedy (D-Mass.) to boost the minimum to \$4.65 over three years. The Bush Administration has countered with a proposal to raise the wage to \$4.25, but insists on a six-month "training" wage for all new workers at \$3.35.

Even if the final bill is closer to Kennedy's version, it's unlikely that the dire picture painted by business will come to pass. Management contends

that the increase will hurt those it is designed to help. The U. S. Chamber of Commerce projects job losses of 750,000 if the wage is increased to \$4.65. But the economic model the Chamber uses doesn't take into account the decline in the number of minimum-wage workers. Nor does it consider all of the 16 states that have raised their own minimum wages above the federal floor. A University of Michigan analysis that uses minimum-wage data through 1986 puts the job loss closer to 70,000.

Even this doesn't guarantee that 70,000 people will be thrown out of work. It simply means that fewer new jobs may be created. And in a labor-short economy, "we're not at all sure

we need those jobs," says University of Pennsylvania economist F. Gerard Adams, who has studied the minimum wage for the AFL-CIO.

COPYCAT HIKE? The decline in the number of minimum-wage workers also makes it less likely that raising the minimum would set off a new wage-price spiral.

Standard economic wisdom holds that a raise in the minimum will ripple up through the wage structure as higher-paid workers clamor for a copycat hike. But with so few workers at the minimum, this ripple may be barely noticeable. That's especially true as the value of the minimum wage declines in relation to average wages: Today it stands at 34.4% of average earnings, compared with 52.2% in the 1960s.

Labor's argument also is questionable. Lifting the minimum is no panacea for the working poor. Only one in five minimum-wage earners lives in a household below the poverty line. Most minimum-wage workers are teenagers or spouses living in families with total income above the poverty level.

Clearly, Congress can help some on the bottom rung with little economic peril. But the lawmakers and the Administration shouldn't fool themselves that they're addressing the real problems facing the poor: the need for better education and job training.



OVERHAULING THE TEAMSTERS

Justice wins direct, secret-ballot elections and a purge at the top

Leaders of the International Brotherhood of Teamsters claimed victory on Mar. 13 when they settled a historic racketeering suit just hours before the trial was to start. The Justice Dept. hadn't appointed a trustee to oversee the union, they crowed, and it hadn't kicked them out of office.

Despite the rhetoric, the clear losers were the Teamsters officials who prosecutors alleged to have ties to the mob. Justice won direct, secret-ballot union elections with permanent oversight by outsiders. And it secured a court-appointed administrator with powers almost as far-reaching as a trustee. As one member of the union's executive board explains: "The administrator is just a trustee by another name."

In addition, most board members with alleged mob links will probably leave. Two such members left in January: Robert Holmes Sr. and Maurice R. Schurr. The settlement includes the removal of two more: Donald Peters is quitting, and Harold Friedman is taking a leave of absence. And board members say that Joseph W. Morgan, Theodore R. Cozza, and Joseph Trerotola plan eventually to resign, although Trerotola denies it.

This would leave only President William J. McCarthy as a board member with alleged mob ties. And union insiders and government lawyers say that he may go, too. Under a lesser burden of proof than is required in court, the administrator can remove McCarthy—or any of the others who don't quit.

OLD GUARD. It all adds up to the first such house-cleaning in 40 years of trying. The feds now may try the same tack with the Hotel & Restaurant Employees, the Laborers' union, and the International Longshoremen's Assn., all of which a 1986 Presidential commission said had Mafia ties.

A key to the government's success was a point often lost in the public debate over the Teamsters: Not all of its leaders are allegedly linked to organized crime. Last summer, Secretary-Treasurer Weldon L. Mathis narrowly lost election to succeed former President Jackie Presser. Although no dissident, Mathis is from Atlanta, where the mob never made inroads. During the election, Mathis embraced reforms similar to those in the settlement—panicking the union's old guard. Led by Trerotola, the 78-year-

old head of the union's Eastern Conference, they orchestrated McCarthy's election, killing the reforms in the process.

Randy M. Mastro, the assistant U.S. attorney handling the case, exploited the split. He began talks with Mathis, seeking his backing for reforms in exchange for being dropped from the case. Mastro also started settlement talks with McCarthy. The ruling faction so feared a Mathis deal that on Jan. 18 it passed a resolution saying that no union officer could agree to a separate settlement.

The feds then drove a wedge between

McCarthy and Trerotola, known as Joe T. They had disliked each other for decades and only teamed up to block Mathis. But once in power, McCarthy undermined Joe T. Mastro demanded the resignations of five board members with alleged mob ties—including Trerotola. McCarthy agreed to go along. In exchange, his resignation wasn't sought.

Mastro counted too much on McCarthy. When he didn't push two deals as he promised, they were rejected. Finally, Mastro reached agreement with Mathis. The feds then asked the judge to rule

against the January resolution, which McCarthy could use to force Mathis of the board. The judge did, dealing the final blow to the McCarthy group.

Many labor leaders feared that the Teamsters suit could be used against clean unions. But the feds have run out most leaders with alleged mob ties while leaving those deemed clean in office. Decades of mob links won't vanish overnight. And McCarthy might hang on. Still, the government made a big win over a union with a tainted past.

By Aaron Bernstein in New York

HEALTH CARE

ON THE SICK LIST: RURAL HOSPITALS

Tighter medicare funding has caught them in a financial vise

For two years, Daniel R. Smigelski has been watching red ink spread through the ledgers of the 80-bed hospital he runs in Lake Village, Ark. His accountants warn him that if Chicot Memorial Hospital has one more bad year, they might recommend closing it. That would force the 4,800 emergency patients it treats every year, from heart attack victims to women in labor, to travel 25 miles to the next hospital—over a bridge that sometimes is closed in winter. "Any number would die," Smigelski says.

Smigelski and other rural hospital administrators blame some of their woes on low reimbursements from medicare, which pays Chicot Memorial only 78% of the cost of treating elderly patients. With the Bush Administration supporting a \$5 billion cut in medicare, country hospitals face even more hemorrhaging. That could set off a budget battle pitting country hospitals against city counterparts, the House against the Senate, and economic efficiency against a widely perceived need for accessible medical care.

STACKED DECK. There's little doubt that many of the nation's 2,600 country hospitals are in trouble. Forty-three of them closed in 1988. And 57% of administrators of rural hospitals say they're at risk of failing within the next five years, according to a survey by Touche Ross & Co., the accounting firm.

The hospitals' troubles took

off in 1984. Before then, medicare payments to hospitals were based on the charges for each case. Now the government pays a set fee for each type of illness. With a big enough caseload, the profits and losses on individual patients should even out. But in a 50-bed rural hospital, a couple of high-cost cases can mean financial disaster. And in the poor communities that many country hospitals serve, there are few patients with paid health plans to absorb those costs.

Making matters worse, country hospitals are paid as much as 40% less than city hospitals for the same treatment. Rural administrators charge that Washington is overestimating the cities' high-

er costs. Complains Eric P. Jensen, administrator of the 37-bed Forks (Wash.) Community Hospital: "Our food costs are higher, we don't get discounts on supplies, and we have to compete for nurses with the larger towns."

One solution, according to supporters of country hospitals, is to have a flat rate nationwide. Such influential senators as Finance Committee Chairman Lloyd Bentsen (D-Tex.) and Minority Leader Robert Dole (R-Kan.) have signaled support for the idea.

FEELING THE PINCH. But a uniform rate could chop urban payments by 2% unless Congress comes up with new funds. And city hospitals, which are also starting to feel the medicare pinch, say they can't spare a dime. Next year medicare payments for both rural and urban hospitals will fall 8% below costs, according to the American Hospital Assn.

Without an accommodation, country hospitals will continue their downward spiral. That doesn't bother some key House members. Representative Fortney H. "Pete" Stark (D-Calif.), chairman of the Ways & Means health subcommittee, argues that more and more small-town patients are abandoning their local hospitals for big city facilities with new technology. "What's great for sentiment and great for hometown pride and great for the local does is probably bad in an economic sense," says Stark.

That won't stop country hospitals from seeking a financial life-support system from Congress, as the budget debate gets under way. While Stark won't oppose a little help for rural hospitals, he says that even doubling the medicare payments won't stop their decline. If that's the case, the country hospital may soon go the way of the one-room schoolhouse.

By Susan B. Garland in Washington



SMIGELSKI: MANY "WOULD DIE" IF HIS ARKANSAS HOSPITAL FOLDED



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THIS HOLLYWOOD LANDMARK COULD BE GONE WITH THE WIND

The fabled Ambassador Hotel is on the block, but so far no one is buying

Charlie Chaplin and Amelia Earhart strolled the grounds. Johnny Weissmuller trained for the Olympics in its pool. The du Ponts and Vanderbilts wintered there, and F. Scott and Zelda Fitzgerald are said to have set fire to their suite's furniture before sneaking out without paying the bill. A vanquished California gubernatorial candidate used its ballroom to tell reporters: "You won't have Dick Nixon to kick around anymore." Now the Ambassador Hotel in Los Angeles, which closed its doors in January, has become a paradoxical white elephant: 23 acres of prime real estate in one of America's hottest markets—which no one seems to want.

After trying vainly to sell it for three years, Chicago's Schine family, heirs to a theater and hotel empire, have decided to put the landmark on the auction block. A first round of non-binding bids is due on June 1. After that, the highest bidders deemed to have enough financial backing will be asked for final offers. Local realtors value it at a relatively modest \$75 million.

WILD CARD. Morgan Stanley Realty, agents for the Schines, says that it has tried to find a buyer willing to preserve the hotel. The firm also talked to developers who want to raze the complex to build offices, stores, housing, maybe even a new hotel. But fears that preservationists would block demolition of the 1921 building cooled their interest. A rumored dispute among the owning family over the hotel's value may also have blocked a sale. One more wild card: The Los Angeles board of education may try to take over the property for a high school.

Yet if those obstacles can be surmounted, the site should lure plenty of developers. Located midway between downtown Los Angeles and Beverly Hills, the hotel sits on the largest undivided parcel of commercial land along busy Wilshire Boulevard. But the neigh-

borhood has fallen from its former glory to "an overdose of minimalls and schlock," says local developer Wayne Ratkovich. Local real estate investors now pin hopes for a revival on redeveloping the fabled Ambassador site. Says Ratkovich: "As this property goes, so goes the neighborhood."

The site already has attracted its share of potential buyers. New York developers W&M Properties Inc., an affli-

building and bungalows that surround into an innovative "urban resort," with conference, health, and recreation facilities. But Jay Rounds of the preservationist L. A. Conservancy admits "it's an uphill battle," and the Schines already have tried for a year to help preservationists find a buyer.

There hasn't been much preservation going on around the Ambassador for some time. These days, the hotel's red carpet is dingy, and its hedges go unpruned. The trademark palm trees of the Coconut Grove nightclub—papier-mâché props from the set of Rudolph Valentino's *The Sheik*—were uprooted long ago. Still alive, though, is a marble fountain in the pillared lobby where Mario Davies rode a horse. John Barrymore once turned a monkey loose at the hotel, and actor Franchot Tone romanced his

wife, Joan Crawford, who in the 1920s walked off with a bunch of trophies from the hotel's dance contests.

Today, the Ambassador is mostly a location for film crews for TV shows, movies and music videos. Among recent visitors were the *Moonlighting* crew and the rock group Guns N' Roses. The Coconut Grove, where the Oscars were awarded in

the 1930s and Benny Goodman and Judy Garland performed, is being rented out by the *Golden Girls* cast to celebrate the show's 100th episode.

The hotel's slide began in the early 1960s, as the Hollywood crowd drifted to tonier hotels in Beverly Hills and downtown L. A. In 1968, when Robert F. Kennedy was gunned down in its kitchen, the

hotel had gotten a bit seedy. When the Schines finally closed the doors in January, about three-fourths of the 500 rooms weren't used because they didn't meet fire standards. Fixing that alone, Volpert says, would have cost more than \$1 million.

The hotel's fate won't be known until this fall, when Morgan Stanley is expected to present the highest bid to the Schines. Then, fans of the Ambassador may know whether this faded belle will get a new lease on life—or, more likely, a date with the wrecking ball.

By Kathleen Kerwin in Los Angeles



IN BETTER DAYS, THE
AMBASSADOR PLAYED
HOST TO THE LIKES OF
FRANCHOT TONE AND
JOAN CRAWFORD



ate of the Malkin family that owns the Empire State Building, unsuccessfully tried in December to buy the property. W&M Vice-President Brian S. Garrison says a dispute among the Schines last December scotched the deal, although the group plans to bid again. Japanese, Korean, and British groups have also met with Morgan Stanley Realty in recent years, says Richard S. Volpert, an attorney for the owners.

On the fringes of a deal as well are local preservationists, who hope to entice someone to save at least part of the sprawling peach-colored stucco complex. Another idea: To transform the main

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PICKENS TAKES AN AX TO MESA DIVIDENDS

► When he converted his company to a limited partnership in late 1985, T. Boone Pickens Jr. vowed to keep his partners happy by paying out steep dividends—and he has. But falling natural gas prices have now forced him to slash Mesa Limited Partnership's dividend by 25%, to \$1.50 per unit per year, starting with the third-quarter payout.

The move should save Mesa about \$41 million annually. Last year, Mesa's cash flow covered only 60% of its \$300 million in dividends. Trading profits and asset sales covered the rest. And in December it acquired \$715 million worth of oil and gas properties from Tenneco, boosting its debt load to an estimated 60% of capital. But Pickens is not about to go broke. He has doubled his gas reserves in two years, making him the king of independents, and he's sitting on \$428 million in cash.

S&L DEPOSITORS DROP OUT IN DROVES

► The thrift industry lost a record \$10.7 billion in deposits in January, compared with an \$8.6 billion drop for all of last year. The Federal Home Loan Bank Board, which regulates S&Ls, says depositors were lured away from the thrifts by money market funds, which averaged 1.25 percentage points above short-term deposit rates at thrifts. While the Bank Board emphasized that planned policy moves contributed to the record outflow, nervousness about the state of the industry undoubtedly played a role, too.

A BROUHAHA OVER 'STOCK BASKETS'

► Spoiling for a fight, the Securities & Exchange Commission approved on Mar. 14 three "stock-basket" invest-

ment products, a new form of security similar to stock index futures. Immediately thereafter, the Chicago Mercantile Exchange and the Chicago Board of Trade filed suit in federal court to overturn the SEC's decision. The futures industry, its exchanges, and its federal regulator, the Commodity Futures Trading Commission, all maintain that the new products are futures contracts, which don't fall within the SEC's jurisdiction.

Meanwhile, two of the stock exchanges that will trade the new investments are squabbling. The Philadelphia Stock Exchange grouches that the American Stock Exchange has stolen its original idea for the baskets. The Amex denies the charge.

ILLINOIS CENTRAL'S EXPRESS TO THE BANK

► One of the nation's oldest railroads has engineered some speedy profits for its investors. On Mar. 10, Illinois Central Transportation Co., owner of the 137-year-old Illinois Central rail lines, accepted a \$20-a-share bid from Prospect Group, a New York leveraged buyout boutique.

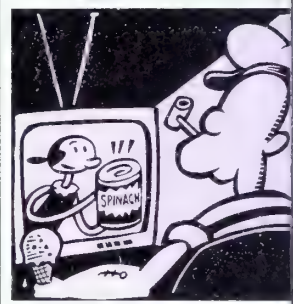
The \$440 million deal marks the end of Illinois Central's brief fling as an independent company. On Jan. 1, Illinois Central was spun off from Whitman, the Chicago consumer products conglomerate.

IF YOU CAN'T TRUST A TOON . . .

Poor Pepsi. It spends millions on an ad featuring Madonna's newest song, *Like a Prayer*. The day after its premiere, Pepsi pooh-bahs blanch when MTV airs the less-than-pious video of the song. Mike Tyson's Pepsi ads were no knockout, either, thanks to his messy divorce from Robin Givens. And you can bet the Beef Industry Council didn't think Cybill Shepherd was a hamburger helper when she admitted she shunned red meat.

But cartoon characters are impervious to sex, drugs, and rock 'n' roll. That's why Betty Boop hawks Hershey chocolates, Olive Oyl sells Solo detergent, and Snoopy pitches Metropolitan Life Insurance.

Still, even cartoon characters have credibility problems. During the seventh-inning stretch at a Mets game last summer, a harried father tried to distract his fidgety child when a Met Life commercial appeared on the scoreboard screen. "Look, it's Snoopy," the parent pleaded. "That's not really Snoopy," scoffed the child. "That's just the insurance dog."



Its shares opened for public trading on Jan. 3 at about 12. So investors who held on to Illinois Central stock appear to have made out like railroad bandits.

LOOSE LIPS CAN BE EXPENSIVE

► William S. Banowsky personified the Establishment. The former university president headed the Los Angeles Chamber of Commerce and advised Ronald Reagan, then governor of California. And he served on corporate

boards, including that of Thrifty, a Los Angeles drug store chain.

In 1986, Banowsky allegedly told family and friends that Thrifty was calling a special board meeting. There, directors considered a buyout proposed by Pacific Lighting, now known as Pacific Enterprises. Allegedly, 18 people traded on that tip and profited when the board approved the deal. Banowsky, now executive vice-president of National Medical Enterprises, didn't benefit, and no charges have been filed against him. But to end a two-year probe by the Securities & Exchange Commission, Banowsky agreed to pay \$754,000 in fines and cooperate with investigators.



A BANANA PEEL UNDER THE U.S. SHOE DEAL

► Two suitors may hold up the sale of U.S. Shoe's footwear division to a Merri Lynch unit. On Mar. 14 the duo—including shoemaker Fisher Camuto Group—said that U.S. Shoe denied them financial data they needed to make a bid. U.S. Shoe replied by casting doubt on Fisher Camuto's financing.



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DOES CHENEY HAVE ENOUGH ARTILLERY TO SCRAP WITH THE BRASS?

Unlike his rejected predecessor, John G. Tower, Defense Secretary-designate Dick Cheney should have no trouble winning Senate confirmation. The Wyoming congressman's difficulties will begin when he crosses the Potomac to take charge at the Pentagon.

The immediate task is cutting at least \$16 billion from the \$26 billion in military spending proposed over the next two years by the Reagan Administration. The budget is likely to cut Cheney, a member of the bipartisan congressional Military Reform Caucus, at odds with the chiefs of the armed services.

The response of the brass to President Bush's budget cuts has been to keep all major programs alive but to spread the saving over a longer period of time, boosting unit costs. "If Dick Cheney wants to make a mark," says one Pentagon civilian official, "he'll send all the budgets back to the services and tell them: 'No more stretchouts.'"

Even more unpopular with the chiefs are reductions in military manpower. The services traditionally have equated troop strength with clout in intense Pentagon budget rivalries and will fight to keep every battalion, ship, and squadron.

The brass can be a formidable adversary, but Cheney has powerful friends. The President himself is pressing the Pentagon to implement reforms. In particular, Bush has been pushing to reduce weapons costs through multiyear contracting. Cheney is also close to National Security Adviser Brent Scowcroft, with whom he worked in the Ford White House.

INEXPERIENCE. The new Secretary will also benefit from the early start by Deputy Secretary-designate Donald J. Atwood, whose nomination is unlikely to be affected by the Toweriasco. Atwood, a former top General Motors Corp. official, is already at the Pentagon, encouraging the civilian officials who hope to put broad procurement reforms in place.

The Cheney team's inexperience in defense matters could be a problem. Cheney did not serve on the House Armed Services committee, and Atwood has no prior government experience. They're going to spend too much time learning," says Russell Murray, a top Democratic aide on the committee. "That means potential for delays and for getting snookered."

Cheney is getting a late start, and dozens of Pentagon positions remain unfilled, including the key jobs of Army, Navy, and Air Force Secretaries. With strong support from the White House, Cheney has a chance to make reform work, but he's going to have to move fast.

By Dave Griffiths

HOUSE REPUBLICANS MAY BE A HOUSE DIVIDED

Dick Cheney's move to the Pentagon solves a big problem for the Bush Administration, but it's a blow to House Republicans. Cheney's exit as House Minority Whip leaves a huge void in the GOP leadership. The result: an ideological struggle in which the ultimate prize is the job of the 65-year-old Republican leader, Robert Michel of Illinois.

Like Michel, Cheney preferred to minimize conflict with the majority Democrats. The favorite to succeed him is House Republican Conference Chairman Jerry Lewis of California, who shares Cheney's sentiments. In December, Lewis won the No. 3 leadership job over Representative Lynn Martin of Illinois. Martin is likely to move into the conference post.

That arrangement would leave Republican Young Turks, who want a more confrontational style of leadership, out in the cold. Representative Newt Gingrich of Georgia, 45, may lead a challenge to the moderate Establishment.

Michel has made no moves to assuage the Young Turks, although he is trying to keep the Old Guard from squabbling among themselves. He recently sounded out Lewis and Deputy Whip Edward Madigan (R-Ill.), another mainstream veteran who wants to move up in the leadership, on a deal. One scenario: Madigan stays out of the whip race, and Lewis agrees not to challenge Madigan for the top job when Michel retires. But unless the old guard can find a bone to toss to Gingrich, Cheney's departure will likely provoke a nasty fight.

By Douglas Harbrecht

CAPITAL WRAPUP

CAPITAL GAINS

The Bush Administration's slim hopes for slashing taxes on capital gains were pinned to a favorable hearing by the Senate Finance Committee. Chairman Lloyd Bentsen (D-Tex.) had indicated he might back the idea if a way could be found to pay for it. But the dream appears to have died on Mar. 14, when the panel gave the plan a frosty reception. Staffers from the Joint Tax Committee told senators the scheme was a big revenue-loser. And ranking GOP member Bob Packwood (R-Ore.) vowed to "do everything I can to stop it" unless the proposal is broadened to add preferential treatment for

timber growers. The Treasury Dept. tacitly acknowledged the legislation's bleak prospects. Secretary Nicholas F. Brady stayed away, sending instead Dennis E. Ross, outgoing Acting Assistant Secretary for tax policy.

HIGHWAYS

Retired Major General Jerry R. Curry didn't get the job he wanted—Veterans Affairs Secretary—but he'll settle for the directorship of the National Highway Traffic Safety Administration. Curry, a black conservative activist, ran unsuccessfully for a House seat from Virginia last year. He also was a supporter of onetime Presidential candidate Pat Robertson.

POLITICS

The next election is nearly two years away, but both parties are picking their Senate targets for 1990. Republicans think their best chance to oust an incumbent is in Iowa, where Representative Thomas J. Tauke is likely to challenge first-term Democrat Tom Harkin. The Republican Senatorial Campaign Committee is urging other hopefuls to leave Tauke a clear field. The Democrats think the most vulnerable GOP incumbent is Kentucky's Mitch McConnell. Polls show Harvey Sloan, McConnell's successor as Jefferson County executive, running neck-and-neck with the first-term senator.

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EUROPE MAY SLAP A QUOTA ON *GENERAL HOSPITAL*

It wants to limit American TV imports—and crack the market open for homegrown shows

On a typical day in Britain, viewers of Sky Channel, the satellite television channel controlled by Rupert Murdoch, tune in such American oldies as *The Lucy Show*, *Three's Company*, and *General Hospital*. On a Saturday in France, children wake up to the antics of Mickey Mouse and fall asleep to the squeals of Betty Boop.

Now, only days after Time Inc. and Warner Communications Inc. announced plans to merge and expand further into Europe, a government-led backlash is setting in. Call it Fortress Culture. On Mar. 13, with the forceful backing of France, the European Community approved a directive stating that European TV stations should devote the majority of their airtime to European-made programming starting in 1990. That will put European producers and film libraries under pressure to come up with hundreds of thousands of hours of programming a year. And as airtime increases with the proliferation of cable and satellite channels following from broadcast deregulation, the demand for new films and shows could more than double by 1995.

CHEAP IMPORTS. Similar to recent decisions that would tighten the European market against imports of Japanese electronic goods, the EC directive attempts to keep low-cost, recycled U.S. programming from dominating Europe's TV screens. Currently, more than 70% of all nondocumentary shows, films, serials, and soaps are imported—and more than 50% of those come from the U.S. The reason is both entertainment value and price. Right now a French TV station can purchase an American television movie for

\$70,000. An original French production runs at least \$1 million. With that price advantage, American producers exported more than \$800 million worth of TV programs to Europe last year. By 1992 they could be selling as much as \$2 billion worth.

Big money is not the only question. Foreign audiences also like the glamour and adventure in the U.S.-made shows.

"It's the attraction of sun, money, success, and beautiful people," says Andre Kaufmann, a television viewer in Frankfurt. But European leaders, especially in France and Italy, deeply resent seeing their audiences glued to American serials from dawn to dusk. The British Broadcasting Corp. and Britain's two commercial channels already restrict non-EC programming to 15% of total air-

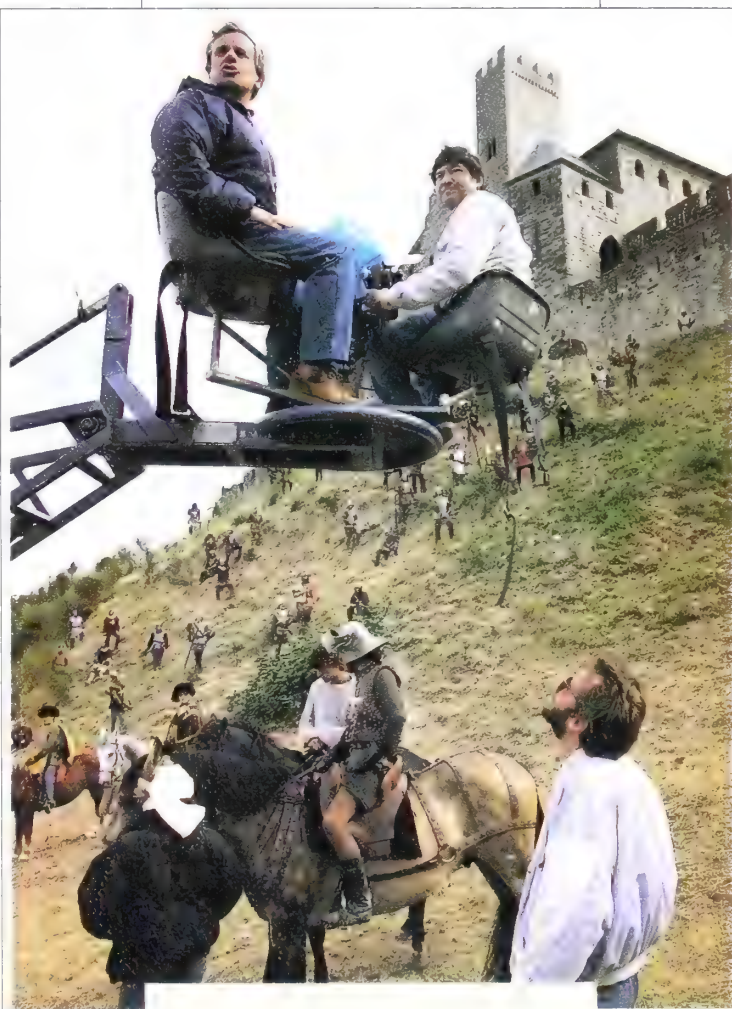
time. France requires 60% of its viewing time to be European, though some stations cheat. French President François Mitterrand, who is spearheading an effort to curb U.S. exports, considers TV a sovereignty issue. Says a Mitterrand aide: "We do not treat culture like any other merchandise."

The EC directive is so vague that it will be months before producers know how strictly it will be enforced. But there's little doubt that it will put European TV stations under pressure to co-finance European programs. Charles Dawson, head of marketing at the European Business Channel in Zurich, thinks that for each extra hour that will be filled with U.S. programs, at least three or four hours will be made in Europe.

Those ratios have suddenly put new life in Europe's media plans. If the ruling holds, the two major roadblocks to Europe's TV show producers, fragmented markets and lack of financing, could be overcome—and a prosperous European-run TV industry

could blossom.

The big players in Europe are already talking deals. Just days after the Time Warner merger was revealed, Silvio Berlusconi, Italy's commercial television magnate, announced that he was holding



French TV crew filming *Joan of Arc*: Mitterrand leads the European cultural crusade

talks with British publisher Robert Maxwell to create a \$1 billion entertainment group. It would produce and distribute TV serials and feature films to be shown across Europe. "We realize we have to do something to remain competitive in an industry where colossal networks are being born," says Gianni Letta, vice-president of Fininvest, Berlusconi's holding company.

Letta explains that the Berlusconi-Maxwell venture was hatched during a December visit by Maxwell to Berlusconi's 18th century villa outside Milan. But the Time-Warner deal accelerated the process. The talks are "in a very advanced stage," says Letta.

Meanwhile, in late February, TF1, the leading French commercial station, 25% owned by French construction tycoon Francis Bouygues, also announced an agreement with Berlusconi and West Germany's Leo Kirch to co-finance European programs. The three are jointly bidding for the five channels on the French satellite TDF1, launched late last year. Canal+, the French pay-TV channel, is setting up a new company with Germany's Bertelsmann to provide a pay-TV service in Germany. The new company is also bidding for channels on TDF1.

These joint ventures will confront the problem of market size. American producers, with a market of 300 million viewers including Canada, can amortize costs a lot faster than their European counterparts. The result: low prices for old material. But European co-production involving different nationalities expands the market right from the start.

NEW BREAKS. To encourage private efforts to develop a TV industry, Mitterrand also has obtained the approval of other European governments to launch a new EC entertainment-subsidy program in September. Producers across Europe will be able to obtain funding from their national governments and the EC for cooperative projects. Even Eastern European countries, which have already provided low-cost facilities for major TV films, will be invited to participate. Mitterrand aides want the plan to be similar to the Eureka subsidy plan that now funds high-tech ventures.

But against all the advantages of the U.S. television industry, the Europeans will not be able to start up a thriving TV industry overnight. For one thing, EC rules would limit commercials to one break every 45 minutes, making time as expensive as the Super Bowl. Yet as the Europeans become more confident, more megawatt shows and fewer ad restrictions are likely to result. If that happens, Europe's entertainment industry will have the makings of a blockbuster.

By Blanca Riemer in Paris and Karen Colman in Rome, with Mark Maremont in London and bureau reports

JAPAN



THE BETTER BUY? A U.S.-MADE F-16 COSTS ABOUT HALF WHAT JAPAN WOULD PAY FOR THE FSX

CAN THE PENTAGON KEEP SHIELDING JAPAN?

The FSX co-development deal is the critical test

When it came to managing U.S. relations with Japan, the Pentagon and the State Dept. used to call the shots. Congress might erupt over Japan's trade practices, and the Commerce Dept. and U.S. Trade Representative might make stern demands, but eventually Washington almost always chose to protect diplomatic and strategic relations with Tokyo.

Now, that bureaucratic power configuration may be shifting, and it carries major implications for U.S.-Japan ties. Growing sensitivity over the U.S. trade position is fueling an increasingly nasty dispute with Japan about developing the FSX, its next generation of fighter aircraft. Commerce Secretary Robert A. Mosbacher and U.S. Trade Representative Carla A. Hills, whose agencies were once bit players in national security issues, are emerging as major forces—much to the distress of both the Pentagon and the Japanese. The interagency squabble could derail plans for Japan to co-develop its new fighter with General Dynamics Corp. President Bush is having to arbitrate the dispute personally.

RICOCHET EFFECT. Far from being just another turf squabble, the bitter FSX fight shows how international economic concerns are starting to supplant cold war tensions as the driving force in Washington policymaking. "We cannot operate in this competitive environment by just giving away our most valuable technology," says William Krist, vice-

president of the American Electronics Assn., which opposes the FSX pact.

If Bush does put new restrictions on the deal, it would be a clear slap in the face to Japan's ruling Liberal Democratic Party and Prime Minister Noboru Takeshita, who is already weakened because of the widening Recruit scandal. Although Tokyo would officially seek to minimize the impact, security, diplomatic, and technological relations between the two countries would be affected. If, for example, Japan wanted to set up a similar co-development scheme for the Navy's P-3 antisubmarine aircraft or the Air Force's Advanced Tactical Fighter, the FSX hassle would not be forgotten.

One key question is whether the new concern over trade will prevail on other sensitive Japanese issues. The 1988 Trade Act requires that Hills identify nations with the most unfair trading practices by Apr. 30, with possible retaliation to follow. The Administration is desperately seeking an excuse to avoid naming Tokyo, even though its trade surplus of \$50 billion is stubbornly high. The Senate authors of the trade law insist Japan be named, whatever the diplomatic consequences. Other fights lie ahead on semiconductors, construction, agriculture, patents, and Japanese acquisitions of U.S. companies.

The FSX fight surprised the leaderless Pentagon at its most vulnerable moment. Japan had wanted to develop its own fighter but the Pentagon last No-

member persuaded Tokyo to enter a co-development scheme involving a technology transfer to General Dynamics.

But opponents argued that Japan could simply buy an off-the-shelf F-16 for \$15 million—about half the per-plane cost of developing a new fighter. As details of the still secret deal began to leak out, suspicions grew that the Japanese might gain valuable computer and systems-integration technology that would help it launch a major civilian aircraft

industry. Some critics argued that overall, Japan would get aircraft technology that cost the U.S. \$7 billion to develop.

The Pentagon and State Dept. are certain to attempt to push the FSX deal through in a form Japan finds acceptable. But even if they do, notice has been served that America's competitive position is developing as a national security issue in its own right.

By Paul Magnusson with Dave Griffiths in Washington and Neil Gross in Tokyo

SOVIET UNION

COLD FEET IN SIBERIA

East-West consortiums haggle over financing for megaprojects

In the offices of Soviet government agencies and the boardrooms of far-flung Western companies, a battle is taking shape that could decide whether the West invests up to \$38 billion to expand the Soviet petrochemical industry. At issue is who should assume the risk for five giant joint ventures that could double Soviet petrochemical exports—and hard-currency earnings—to the mid-1990s. Led by Combustion Engineering Inc., the Western companies

goods, but that could take until the next century. Meantime, the Soviets want to upgrade their crude oil into more valuable petrochemical exports such as polyethylene. Such companies as Occidental Petroleum, Italy's Montedison, and Japan's Mitsubishi Corp. have all stepped up to participate (table). But they are wary of Soviet operating costs, which can be double those in the U.S., and of other Soviet economic troubles. Says CE Vice-President Maxwell Asgari: "It's one

antees covering their own share of the ventures. But the CE group "will not under any circumstances" do that, Asgari says. CE is in no shape to take on added risks after posting a \$245 million after-tax loss on 1988 sales of \$3.5 billion.

Still, says a U.S. banker involved in Soviet trade, "if I were the Soviets, I would not guarantee 100%. Certainly Oxy. Combustion, or McDermott have facilities to raise financing on their own and be responsible for the projects up to a point." Inside the Soviet Union, debate has erupted over whether to supply guarantees and what institutions might offer them. The Soviet Bank for Foreign Economic Affairs could strain its credit rating if it guarantees the projects and has to back up the pledges with hard currency. But industrial ministries don't have the financial muscle either. The Soviets hope that European or Japanese export credit agencies will help guarantee the projects.

STRAIN. If the Soviets and the CE consortium can agree, construction on the projects could begin this summer. The group proposes to build complexes costing \$2 billion to \$10 billion each at Surgut and Tobolsk in Western Siberia. Each plant would make such products as gasoline additives and synthetic rubber. Meanwhile, negotiations continue on the other ventures. Britain's John Brown PLC says it may join McDermott to build a plant

to produce 200,000 to 600,000 tons of polyethylene a year. The first stage alone will cost \$500 million.

Given the magnitude of the projects, however, it's most likely that the Soviets will have to scale back their ambitions and carry out just two or three ventures. Building all five would strain both the willingness of foreign lenders to finance them and the capacity of world markets to absorb their output. "[The Soviets] will probably pick and choose those projects

THE SOVIET PLANNERS' FIVE TOP PETROCHEMICAL PROJECTS

Site	Partners	Estimated cost Billions of dollars
SURGUT, SIBERIA	Combustion Engineering and McDermott; Japan's Mitsubishi and Mitsui	\$5 to \$10
NIZHNEVARTOVSK, SIBERIA	Japan's Mitsubishi, Mitsui, and Chiyoda Corp.	\$5 to \$10
TOBOLSK, SIBERIA	Combustion Engineering and McDermott; Japan's Mitsubishi and Mitsui	\$5 to \$10
TENGHIZ, KAZAKHSTAN	Occidental, Italy's Enichem and Montedison, and Japan's Marubeni	\$6
NOVOYE URENGOY, SIBERIA	McDermott and other Western partners	\$2

DATA: ENI



SIBERIAN WELLS: WILL THE SOVIETS GIVE GUARANTEES?

want the Soviets to take on most of the risk—and offer the government guarantees to attract bank financing. Says Richard Dean, a Moscow-based lawyer with Coudert Brothers, a New York law firm: "The credibility of the Soviet Union for big capital investment is at issue."

The Soviets need the petrochemical ventures to fit a gap in President Mikhail S. Gorbachev's timetable for revamping the Soviet economy. The Soviet goal is to boost exports of manufactured

thing to put \$3 million into the Soviet Union. It's another to put in \$3 billion." CE already has a small joint venture to upgrade Soviet refineries.

NO ADDED RISKS. In recent weeks, CE and its partners—McDermott, Mitsubishi, and Mitsui & Co.—have held intensive talks with Soviet officials in Moscow and in London. Another round began on Mar. 15 at CE's Stamford (Conn.) headquarters. Asgari says the Soviets want the Western companies to provide guar-

that will earn hard currency the quickest." says Michael W. McCorkle, head of First National Bank of Chicago's Eastern European unit. With earnings from traditional exports of only \$30 billion last year, the Soviets face a hard-currency crunch. That may leave them little choice but to swallow hard and give Western companies at least some of the guarantees they want.

By Peter J. Daniels in Moscow with Paul Kling in Shanghai, China, and Bureau reports

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GORBACHEV'S NOT-SO-SECRET WEAPON: THE BALLOT BOX

To survive politically and push his reforms, Mikhail S. Gorbachev has had to outflank entrenched bureaucrats with varied stratagems, from decentralizing ministries to orchestrating a special Communist Party conference last year. On Mar. 26 he will complete an even bolder end-run around conservative opponents with the Soviet Union's first contested elections since the Bolshevik Revolution's earliest days. The elections will create a new legislature, the Congress of People's Deputies, with 2,250 members. With this political body, representing an electorate of 180 million voters, Gorbachev plans to offset the political power of the Central Committee of the Communist Party, which represents an elite of 9 million members.

"This, of course, will strengthen Gorbachev," says Roy A. Medvedev, the disident historian, who is one of 3,645 candidates for seats in the Congress. Gorbachev now wields power as the Communist Party's General Secretary. With the new Congress, he will also be the Soviet Union's chief executive. First, the Congress will choose from its own membership a 552-member Supreme Soviet to serve as the country's working parliament, with power to initiate and debate legislation. Unlike rubber-stamp Supreme Soviets of the past, this body will have real power. In turn it will elect an executive body, or presidium, whose chairman undoubtedly will be Gorbachev. The new structure will make Gorbachev seem more like a Western political leader with a mandate from the people. Recalling the 1964 ouster of former leader Nikita Khrushchev, a Western diplomat says: "The election will make it more difficult for [party opponents] to do to Gorbachev what Leonid Brezhnev did to Khrushchev."

More important for Gorbachev right now, the election—and others to be held next fall for regional and local legislatures—providing an unprecedented public platform for *perestroika* supporters. Debates are airing issues from food shortages to

inflation and the environment. Still, the campaign falls short of Western democratic norms—or even of the example of Poland, which plans free elections for a new upper house of parliament. In the Soviet Congress, 750 seats are reserved for unopposed candidates of the party and groups such as unions. For some of the remaining 1,500 seats, candidates were hand-picked by political bosses such as the Ukraine's Vladimir Sherbitsky. But many seats are hotly contested. In one Moscow district there are 12 rival candidates, and overall, voters are likely to send a disparate mix of legislators to the Congress, from Baltic nationalists to Moscow populist Boris N. Yeltsin. About 85% of all candidates are Communist Party members, but many are rank-and-file reformers, politically at odds with conservative party *apparatchiks*. "They are only formally members of one structure, one party," says Lev Timofeyev, who edits an independent newspaper. In next fall's elections, he suggests, "there will be more opportunities for truly independent people."



IN MOSCOW, A CHOICE, NOT AN ECHO

IMPROVISING. The new Supreme Soviet is expected to hold two four-month sessions each year, unlike predecessors which met for only a few days. But to gain independent clout, the legislature may have to evolve structures such as the standing committees of the U. S. Congress, with expert staffs to advise members and draft legislation. Says a Western diplomat: "They are making up the rules and plans as they go along."

Gorbachev has improvised many steps on his journey away from orthodox Communism, but his basic direction has not changed. He still faces bruising battles, such as Central Committee resistance to his plan for shifting Soviet agriculture to family farming. His strategy has been to enlist public voices against such opposition within the party. Now, by bringing outsiders into revamped legislatures, Gorbachev aims to institutionalize these pressures for change.

By Peter Galuszka in Moscow, with Gail Schares in Bonn

GLOBAL WRAPUP

WEST GERMANY

Chancellor Helmut Kohl's troubles are underscored by the drubbing his center-right coalition took in municipal elections in Hesse state on Mar. 12, after a Jan. 29 defeat in West Berlin. Kohl's Christian Democratic Party picked up only 33.5% of the vote statewide, down from 41.1% in 1985. And in Hesse as in West Berlin, Kohl's junior coalition partner, the Free Democratic Party, failed to win the 5% vote needed to qualify for seats in Parliament.

The election shows a continuing polarization between the Social Democratic Party and environmentalist Greens on the left and radical-right

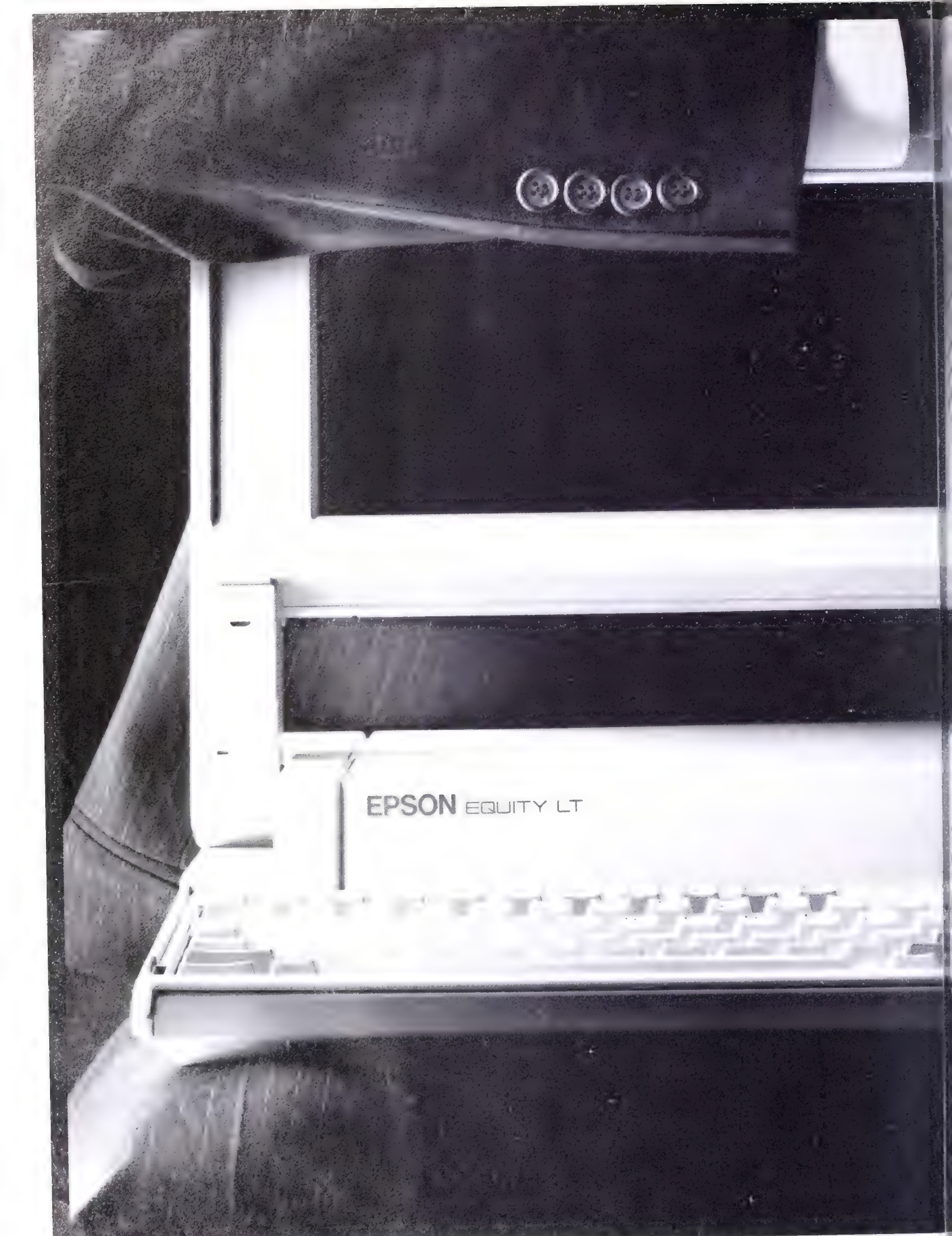
groups. The right-wing National Democratic Party vaulted to 7% of the vote in Frankfurt, up from zero in 1985. That registered a backlash against an influx of foreigners and against Kohl's proposals to cut health and pension benefits and reform taxes. Up to now, a strong economy has benefited Kohl. But if it slows, his prospects could plummet.

LATIN AMERICA

A U.S.-Latin deal settling a two-year dispute over decision-making in the Inter-American Development Bank will open the way for a \$22 billion boost in the bank's lending power and bolster U.S. efforts to ease the

Latin debt crisis. The U. S. puts up 75% of the bank's funds but has only 35% of the voting power. Latin countries have 54% of the vote, with the rest wielded by other contributors.

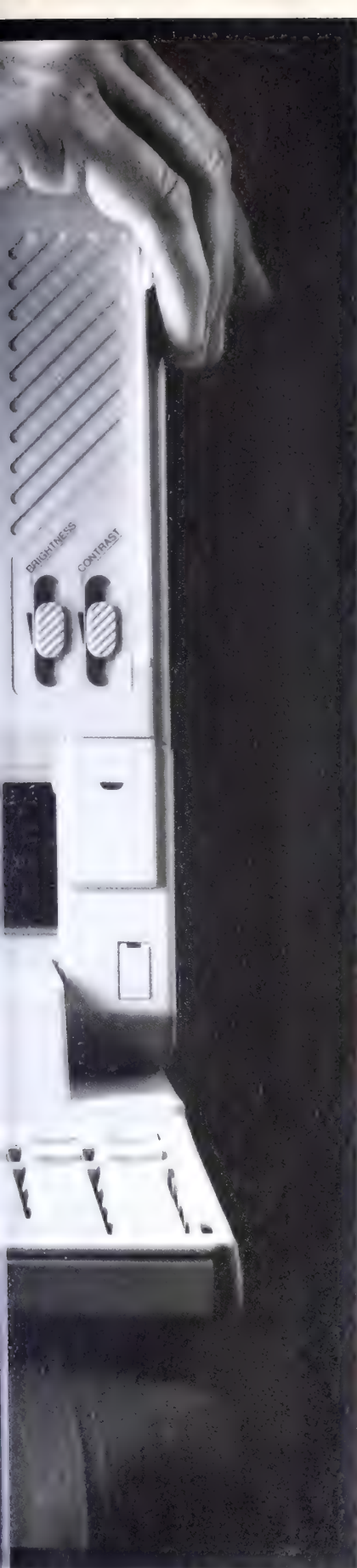
Washington wanted the right to veto loans in order to shift the bank's emphasis from financing projects such as roads and dams to using its leverage to spur economic reforms it says are badly needed. But Latin American officials feared that the U. S. would use its veto politically to punish Nicaragua and other countries out of favor with Washington. A compromise will allow a loan to be delayed for as much as a year if two of the bank's 12 directors favor doing so.



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KELLEY: AFTER A RIVAL TRIED TO "SQUISH HIM LIKE A BUG," A JURY AWARDED \$6 MILLION

PUNITIVE DAMAGES: HOW MUCH IS TOO MUCH?

The Supreme Court could soon curb runaway jury awards

In 1987, Joseph Kelley hit the jackpot. Seven years earlier he had left a Browning-Ferris Industries Inc. subsidiary in Burlington, Vt., and started Kelco Disposal Inc., to compete with his old employer hauling industrial trash. Soon the local Browning-Ferris manager was told to "put Kelley out of business. Do whatever it takes. Squish him like a bug." When Kelley filed an antitrust suit against the No. 2 U.S. trash hauler, Browning-Ferris backed off—and even left town. Kelco won just \$51,146 in actual damages. Then came the shocker: With Kelley's lawyer imploring the jury to "deliver a message," it assessed \$6 million in punitive damages.

Whether Kelley ever gets his money depends on how the U.S. Supreme Court rules, probably by July. But the message has been delivered. Everyone from manufacturers to Wall Street brokerages to the U.S. Chamber of

Commerce is rallying to Browning-Ferris' side. They've filed briefs in support of the garbage company's contention that huge damage awards violate the Constitution's Eighth Amendment prohibition against "excessive fines." This principle has long been accepted in criminal cases, but never in civil suits.

Meantime, two other big losers—Goodyear Tire & Rubber Co. and Metro-media Inc.—are asking the high court to overturn lottery-size punitive damages that have been levied against them. A

victory in any of these cases would help set guidelines to curb the size of punitive awards, perhaps the biggest legal headache a company can face.

Business tends to get hyperbolic when discussing punitive damages, but perhaps understandably. In 1987 a jury in Belleville, Ill., awarded just \$1 each to 65 plaintiffs after a spill of a wood-preservative product made by Monsanto Co. leaked fumes into their town. Then the jury slapped the St. Louis company with \$16 million in punitive damages. Last year, a Minnesota jury awarded \$12.5 million in punitive damages, later lowered to \$4 million by the state supreme court, to a man injured when a 25-year-old, two-piece tire rim made by Goodyear separated with explosive force as it was being mounted on a truck.

HIDDEN TAX. Critics of high punitive damages argue that the effects of such awards spread far beyond the individual case. A recent Insurance Information Institute study found that the threat of punitive damages results in the "upward ratcheting of settlements" by insurers. That pushes up insurance rates, creating what Peter W. Huber, a lawyer and author of the recent book *Liability: The Legal Revolution and Its Consequences*, calls a hidden tax on products that hurts America's international competitiveness. Huber puts this tax at \$80 billion a year.

Such estimates are adding steam to an old debate. The concept of punitive damages arose in the late 1700s, but awards were rare and relatively small until the 1960s, says David G. Owen, a University of South Carolina law professor and leading theorist on punitive damages. In the early 1980s, after an explosion of product-liability suits, the awards suddenly soared and spread beyond mere product claims.

Now, business, which had unsuccessfully challenged punitive damages on constitutional grounds in the 1960s, has renewed its assault, with better luck.

Owen points to a Mar. 9 decision in New Jersey that he says was the first time a federal court had found any aspect of punitive damages unconstitutional. The court said that multiple judgments against the same company for making or selling harmful products violate the 14th Amendment's guarantee of "fundamental fairness."

Defenders of big awards argue that the

FIVE OF THE LARGEST PUNITIVE DAMAGE AWARDS

	Award
1978 A California jury awards Richard Grimshaw and others punitive damages from Ford Motor over defective Pinto gas-tank design	\$125 MILLION
1986 A Texas jury awards William and Shirley Durrill punitive damages from Ford Motor over defective Pinto gas tank design	\$100 MILLION (reduced to \$10 million)
1987 A Delaware jury awards three couples punitive damages from Raymark Industries for conspiring to hide asbestos risks	\$75 MILLION*
1987 A Kansas jury punishes Allied-Signal Inc. for predatory practices leading to General Poly Corp.'s bankruptcy	\$60 MILLION*
1987 An Illinois jury awards the Federal Deposit Insurance Corp. damages from W.R. Grace for fraudulently securing a loan	\$75 MILLION (reduced to \$25 million)*

*Appeal pending

DATA: BW



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threat of them keeps products safer and companies more honest. "You're punishing wrongdoers," notes Joan Claybrook, president of Public Citizen, a consumer-advocacy group. Moreover, analyses of federal and state court rulings have shown that punitive damages are relatively rare. And the Association of American Trial Lawyers, the people who mostly bring damage suits, estimates that only 110 awards in the past 30 years have exceeded \$100,000.

But that's small comfort to companies that get hit hard. They argue that guidelines are in order both for juries and for state court judges, who hear the majority of punitive-damage cases. Richard Neely, a West Virginia judge and author of *The Product Liability Mess*, says that many judges, under tremendous community pressure, seek "elaborate ways to make business pay for everyone else's bad luck."

'TAR BABY.' Certainly, that's what business is claiming in the cases before the high court. Browning-Ferris' lawyers think if Kelley is given punitive damages at all, they should be tied to the real losses he suffered, not to Browning-Ferris' \$1.3 billion in revenues, as Kelley's lawyer urged. And Goodyear, invoking due process protections, argues that it shouldn't be so severely punished when it had no idea it could be held responsible for such an old product.

There are few clues as to how the high court might lean: In the past decade it has twice ducked the issue. "To get involved is like hugging a tar baby," says Richard A. Epstein, a University of Chicago law professor. "Conservative justices will be reluctant to use constitutional law to intervene in an historically states' rights area, and liberals will be wary of interfering with justice."

To hedge its bets, business is augmenting its legal attacks with aggressive lobbying. Since the mid-1980s, some 41 states have curbed "pain and suffering" awards, raised the burden of proof for punitive damages, or curtailed the rights of plaintiffs to sue more than one company for the same injuries. And 12 states have capped product liability awards. Now business wants more. It is pushing for exemptions for products that comply with government standards. And it wants punitive damages to be awarded in separate trials.

In Burlington, meanwhile, Joseph Kelley ponders his own damages. Kelco Disposal has recovered and is prospering. But Kelley, 58, says that doesn't make up for the trauma of selling his house and having his wife return to work to pay his legal bills. Now he would like to even the score. Kelley says \$6 million sounds about right. "It's a lot of money to me but not a whole lot for them."

By Elizabeth Grillo Olson in Washington

People

SURGEONS

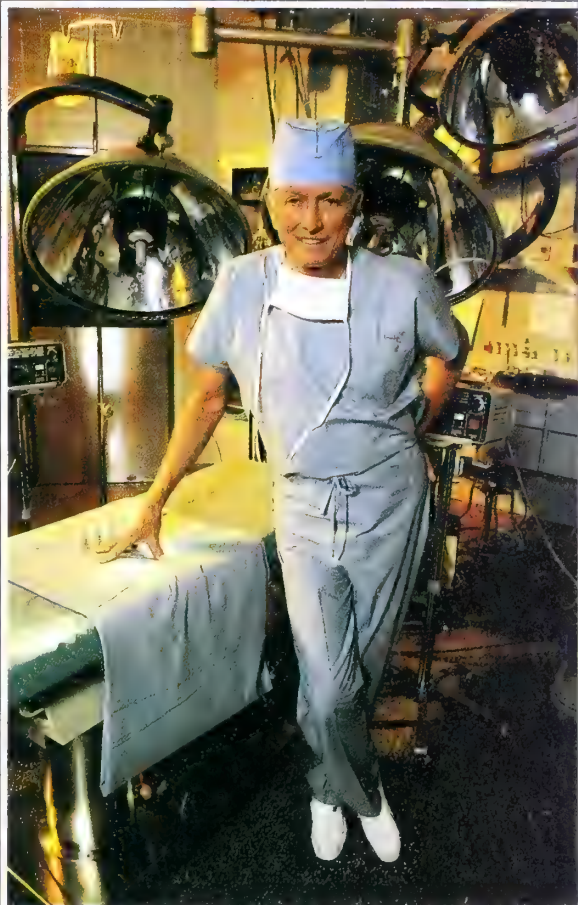
WILL DENTON COOLEY MAKE MEDICAL HISTORY AGAIN?

This time the surgeon is pioneering cut-rate heart bypasses

When Denton A. Cooley arrives, his patient already is face up on the operating table, chest cavity stretched wide apart by two splints. Using scalpel, scissors, and thin wire, Cooley begins stitching in new arteries to replace older, clogged ones. Under the glaring lights, his long, slim fingers move swiftly and silently. Two hours later he has finished a triple-bypass operation. Without a word, he rips off his bloody gloves and slides out the door, leaving others to sew up the chest. Marvels one assistant: "I've seen other surgeons take six hours for that operation."

Well, you know what they say about practice. In 30 years, the Houston doctor and his team of surgeons have performed 80,000 heart surgeries, more than anyone else in the world. He pioneered the first American heart transplants and implanted the first artificial heart in a human. But 20 years after that feat, Cooley, 68, is facing some heart-stopping challenges of his own. He's trying to recover from personal bankruptcy, brought on last year by the failure of several commercial real estate projects. Meanwhile, he is struggling to stay on top of a field teeming with new competition. Cooley has dominated his specialty for years. Now hundreds of smaller hospitals have cut into his practice. From 1980 to 1988, the number of open-heart surgeries at the Texas Heart Institute (THI)—the research organization housing his private practice—dropped 39% (chart, page 58). During the same period, open heart surgeries in the U.S. tripled.

Cooley's comeback strategy is a lot



RIVALS SAY COOLEY'S PLAN SMACKS OF SOCIALIZED MEDICINE

like Sears Roebuck's: everyday low prices. He is aggressively marketing a cut-rate service that he claims will save health care providers millions of dollars. Under his "bundled" service, patients and insurers can pay for everything with one fee—instead of separate bills for hospital expenses, surgeons, and other specialists. At about \$15,000 for a standard bypass, Cooley's service costs some 40% less than the national average.

ASSEMBLY LINE. Medicare is interested. A study by the Inspector General's office, which oversees U.S. health agencies, showed that Medicare could cut its \$1.5 billion annual bill for heart surgeries by 13%—even if it meant flying patients into Houston and housing them. Medicare soon will test flat fees in

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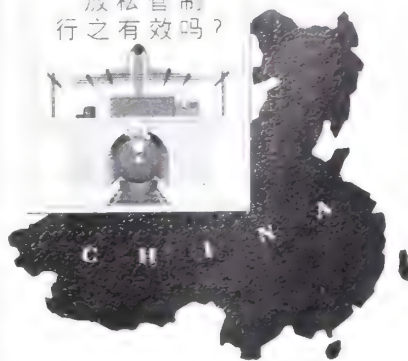
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People

pilot program in four or five hospitals, to be named by this summer, with an eye toward building a national flat-fee system. If it is chosen, as expected, THI should draw thousands of new patients, pushing it far ahead of the pack. Says THI Executive Director Charles E. Edmonds: "It'll prove that our program makes sense."

But many hospital officials and doctors will probably resist any plan that costs them patients. That's especially true now that medicare has instituted diagnostic-related groups (DRGs), a fee structure limiting the amount a hospital can collect for most procedures. "Many doctors see [a flat-fee system] as nothing more than socialized medicine," says Michael Hupfer, an official with the Health Care Financing Administration, which oversees medicare.

It's not as if Cooley needs extra work to keep himself busy. He continues to perform six to eight surgeries a day—and swears he has no plans to quit.

Working 12 hours at a stretch, five days a week, he breaks only for brief lunches in his office, located deep in the confines of St. Luke's Episcopal Hospital. In all, his team of five surgeons handles 35 to 40 operations a day. Cooley derives up to 30% of his income from work performed by others at THI—which explains why he wants to boost volume. Some rivals think his assembly line already is running too fast. But Cooley will have none of that: "If it's an assembly line, it's a Rolls-Royce line." He points out that nearly 90% of his bypass patients live five years and 74% make it 10 years.

CRASH LANDING. Cooley has always been good with his hands. The son of a Houston dentist, he starred in basketball in high school and at the University of Texas. He then attended Johns Hopkins University's medical school. In 1951 he joined the Baylor College of Medicine with famed heart surgeon Michael E. DeBakey. All went well until 1969, when Cooley implanted the world's first artificial heart in a human. That infuriated DeBakey, who felt the device was his invention, associates say. Cooley argues that DeBakey was just jealous he didn't get to use it first. That year, Cooley left to join St. Luke's, where he founded THI. He and DeBakey haven't spoken since.

Although he keeps long hours, Cooley takes a little time out. He likes to spend weekends with his three grown children and 12 grandchildren. He plays tennis

and golf and used to play bass fiddle in a band called the Heartbeats. He even authored a cookbook featuring low-sodium recipes, which has sold 70,000 copies. He's soft-spoken with a dry sense of humor, and he rarely loses his cool. One exception is when his staffers can't accommodate his tight scheduling needs. "He doesn't realize that everybody can't spend all their time at the hospital," says one doctor.

Until the Houston economy crashed, Cooley's biggest concern was how to invest all his money. But when he filed for Chapter 11 protection last year, he owed 200 creditors about \$97 million. Under

his bankruptcy plan, they will be paid back in five years, mostly from asset sales. Cooley was able to protect most of his \$9.7 million-a-year salary, his \$1 million mansion, and his 489-acre ranch. He also was able to buy back his two Galveston beachhouses and two Rolls-Royces from his estate.

Even some of his hospital colleagues

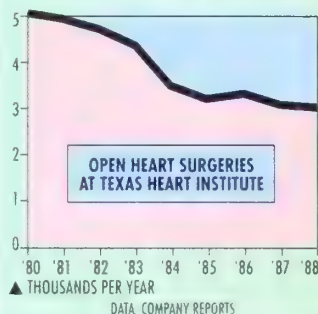
think he got off too easy. "When he's making \$9 million a year, it's hard to feel sorry for him," says an associate. Cooley insists he didn't want to file Chapter 11, but his creditors gave him no other option: "They wanted me to be their slave."

NINE LIVES. If he is a slave to anything these days, it is building THI. The institute already has signed up 18 companies and health maintenance organizations for the flat-fee service, accounting for 6% of its business. Cooley is also pushing ahead on the technological front. The most promising new devices are small pumps that, when implanted, replace the heart's pumping action. But they must be hooked to an outside machine, so they're mainly used to keep patients alive until donor hearts can be found. THI, which has transplanted 300 hearts since 1982, has a long list of waiting patients. And a true battery-operated artificial heart is thought to be years away. So heart disease is expected to remain the No. 1 killer in America.

Despite Cooley's hurried pace, his patients seem happy as ever. As he checked on one bedridden patient recently, the man's wife asked Cooley for an autograph. She then offered that he had just saved her husband's life for the second time. "A cat has nine lives," the doctor said. "Maybe your husband does, too." For that matter, so might Cooley.

By Mark Ivey in Houston

COOLEY: LESS SURGERY



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A DRUG THAT COULD REPLACE TRANSFUSIONS —IF IT EVER REACHES THE MARKET

Ortho is asking for a delay of Amgen's EPO, a promising dialysis aid

It's a bit like being sued for divorce just as you're entering the delivery room. The Food & Drug Administration approval that will allow Amgen Inc. to begin selling a promising gene-spliced drug called erythropoietin, or EPO, has hit the "any minute" stage. But in the frenzy of last-minute details that accompany the long-awaited rush to market, the Thousand Oaks (Calif.) biotech company must also cope with a broadside lawsuit by its corporate partner, Johnson & Johnson's Ortho Pharmaceutical Corp.

In late January, Ortho asked a Delaware judge for an injunction delaying marketing of the drug until a dispute over joint-venture terms is settled. A hearing is scheduled for Mar. 17. The suit shocked analysts and industry executives alike—especially coming from a company whose corporate creed proudly states that its "first responsibility is to doctors, nurses, and patients." Says PaineWebber Inc. analyst Linda Miller: "Trying to keep a drug off the market is the antithesis of what you expect an innovative drug company to stand for." Philip J. Whitcome, chief executive of biotech company Neurogen Inc. and a former executive at Amgen, says: "It's like holding the patients hostage."

BLOOD BOOST. The suit caps several years of growing rancor between Ortho and Amgen over EPO's future. In the early 1980s, Amgen scientists used gene-splicing to produce large quantities of EPO, a natural protein that stimulates the body to produce red blood cells. It can repair the severe anemia that afflicts up to 120,000 kidney dialysis patients. The only alternative therapy is a blood transfusion. EPO may also prove to be enormously useful for many forms of anemia, including that caused by the AIDS drug AZT. Someday, surgery candidates who want to bank their own blood could use EPO to replenish their red blood supply.

Ortho, which was also eyeing the drug, cut a deal with the fledgling biotech company in 1985. At the time, Amgen's fortunes were floundering and its stock was bobbing around 7. So it agreed to license EPO to Ortho, retaining the right to manufacture and market

it only for use by dialysis patients.

The problem, says analyst Teena Lerner of Shearson Lehman Hutton Inc., is that "neither company thought the drug would be that big." Nor did market observers believe that tiny Amgen would have the resources to beat Ortho through the lengthy and costly clinical testing process required for FDA approval.

Wrong on both counts. Lerner says the Street's most bullish analysts on EPO, is convinced it will command a \$2 billion market (charged by Amgen). Although Amgen Chairman George B. Rathmann has publicly urged caution in those estimates, there's no question it will be a blockbuster. In addition, the tiny startup beat the pharmaceutical giant through the FDA

SPILLOVERS. Ortho watchers say the company did not move quickly to initiate non-dialysis clinical trials or pull together the required documents to start the approval process within the FDA. Nor did it plan early enough for a manufacturing operation to produce EPO. Ortho's lawsuit, however, claims that Amgen was deliberately uncooperative and did not make available product materials and information that would support such a filing.

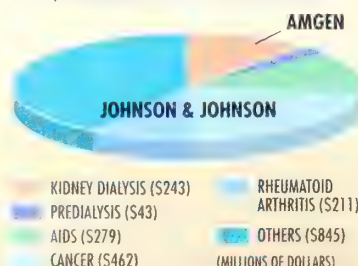
Now, with FDA approval of EPO for Amgen expected by the end of the month, Ortho is afraid it will lose out in the non-dialysis markets. Since physicians routinely prescribe drugs for applications outside their approved

uses, Ortho fears they will simply use Amgen's product to treat other forms of anemia. Ortho's lawsuit contends that until its product is approved for non-dialysis uses, which is not expected until well into 1990, Amgen will unfairly profit from those "spillover sales."

J&J officers declined to comment on the suit, but Ortho attorney David F. DeBans told the court that Amgen would have gone broke without Ortho's EPO and that the company tried to resolve the differences in negotiations. "No



THE BATTLE OVER EPO \$2 BILLION POTENTIAL MARKET



DATA: SHEARSON LEHMAN HUTTON INC.

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hat success is at hand," he stated, "Amgen seeks to deny Ortho the fruits of its bargain." Responds an Amgen spokesman: "We believe we've adhered to the contract. We were totally surprised and find it unusual that they were trying to keep a drug off the market for which there is no alternate therapy."

ORPHAN STATUS. Despite the controversy, Amgen's stock has held steady above \$8. That's because most observers expect the matter will ultimately be resolved in arbitration by awarding Ortho some percentage of Amgen's sales to hemodialysis patients until the larger company wins approval of its product. And they do not expect the FDA to let the dispute impede the approval of Amgen's EPO.

Indeed, the agency has already refused to hold up EPO for another non-medical reason. Senators Edward M.

Few expected tiny Amgen to win FDA approval first. Now its venture partner Ortho wants to cut a new deal

Kennedy (D-Mass.) and Orrin G. Hatch (R-Utah) threatened EPO's progress as they tried to hammer out a change in the so-called orphan drug law, under which Amgen has rights to market the drug to dialysis patients without competition for seven years. The senators asked the FDA not to award exclusivity to Amgen's EPO until at least June 30, while they wrote legislation to fine-tune the law. However, FDA Commissioner Frank Young responded that he could not separate such a move from the approval process, especially since the drug was "virtually approved."

The senators believe that drugs with huge potential, such as EPO, should not qualify for orphan drug status, which seeks to make available potentially unprofitable drugs. And if they succeed in changing the law, it would be just what the doctor ordered for another partnership—Boston's Genetics Institute Inc. and Japan's Chugai Pharmaceutical Co.—that is also seeking approval for EPO. So instead of spewing venom, Amgen and Ortho might be better off standing shoulder to shoulder against looming competition that could cost them both dearly. But as their marriage continues to crumble, it looks as if it's up to the courts and the FDA to see that desperate patients get this drug.

By Joan O'C. Hamilton in San Francisco and Joseph Weber in Philadelphia

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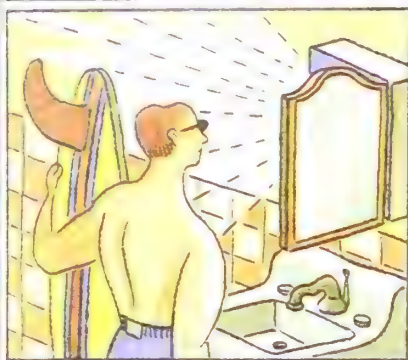
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EDITED BY NAOMI FREUNDLICH

THIS HORMONE MAY GIVE YOU WHAT THE SUN CAN'T: A SAFE TAN



Cancel your appointment at the tanning salon, throw out your tickets for the Caribbean, and put away your foil reflector. "You can be in a dungeon and still get a tan," says University of Arizona researcher Mac Hadley. He's talking about a synthetic hormone that could some day

stimulate pigment-producing cells, called melanocytes, to bring out a tan without the dangerous effects of ultraviolet rays. Melanotan, as the synthetic hormone is dubbed, is modeled after the one that changes the camouflage colors of chameleons, rabbits, and frogs. "Our molecule is 1,000 times more active than the natural hormone, because it is not broken down as fast," says Hadley, an endocrinologist.

Humans probably lost the melanocyte-stimulating hormone as they evolved, Hadley says, but there are still receptors for the hormone on the pigment cells. Preliminary results from human tests—the hormone is applied via a skin patch—indicate that it is safe in low doses. Several more years of testing and formulating are necessary before Melanotan will be ready to market, but Johnson & Johnson's Ortho Pharmaceutical Corp. is now footing the bills.

IT INSULATES, IT FIREPROOFS—AND IT'S NOT ASBESTOS

Residential and commercial builders have long searched for an insulator that's virtually fireproof while producing no health or environmental threats. Researchers from Georgia Institute of Technology believe they've found the answer in tiny ceramic bubbles. The bubbles, which are formed in a liquid slurry, are heated to form hollow ceramic spheres that are lightweight, durable, and capable of withstanding temperatures hotter than 3,200F. By comparison, fiberglass insulation withstands temperatures only up to 800F.

The ceramic spheres—which are as small as 1.5 millimeters in diameter—can also be bonded together to form boards to insulate super-hot equipment in steel or petrochemical plants. And Joe K. Cochran, head of the Georgia Tech research team, believes hollow bubbles of different sizes have many uses—for example, as a support for catalysts in chemical manufacturing or even for encasing time-released medicines.

MORE GOLD MEANS BETTER CONNECTIONS FOR MICROCHIPS

Members of Microelectronics & Computer Technology Corp. (MCC), one of America's pioneer research consortiums, now see the glint of a payoff: a way to attach hair-thin gold wires to any part of a microchip, not just its edges.

That's important because of the ever-growing complexity of chip designs. Today's tiny silicon chips need more and more links to the outside world for sending and receiving data. But

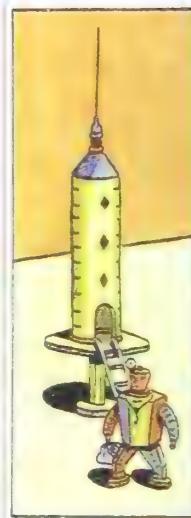
the edges of many chips are already packed to capacity with so-called leads, the ends of gold wires—and soldering them elsewhere poses the risk of damage from heat.

After three years of work, MCC's researchers have developed a laser-based technique that does the trick with virtually no danger of harm from heat. In the lab, MCC has produced chips with 400 leads, more than triple the number on any existing chip. The technology for building the new chip-bonding machines has been licensed to Electro Scientific Industries Inc., a supplier in Portland, Ore., that expects to have a commercial version ready by yearend. For the first two years, MCC's 19 shareholders will have first dibs on the machines.

SUBMARINES SMALL ENOUGH TO CRUISE THE BLOODSTREAM

Remember that 1966 movie where Raquel Welch was part of a medical team that gets shrunk to the size of bacteria, then navigates through the arteries of the proverbial great scientist to perform surgery on—or rather, in—his brain? Everyone knows you can't really shrink people, but scientists at Tokyo University are going after something straight out of *Fantastic Voyage*: an ultraminiature submarine that can be launched into a person's bloodstream.

Professor Iwao Fujimasa, whose specialty is artificial heart technology, hopes to have a prototype of the robotic sub ready in about a year. Building it will require gears and other parts far smaller than anything yet carved from metal. They will be made by so-called micromachining techniques—now used for etching circuit lines in semiconductors. The sub would also have to be equipped with ultratiny devices for inspecting suspect tissue and relaying the findings to doctors, who might then direct the robot to cut out or treat any diseased parts. If the team can pull the technology together, "there are thousands of other applications," says Fujimasa.



A CALCULATOR FOR THOSE WHO WOULD RATHER WRITE IT OUT

Japan is under tremendous foreign pressure to deflect its export juggernaut by stimulating domestic demand, and Canon Inc. evidently aims to oblige. Last month the Tokyo company introduced a \$500 calculator designed expressly for Japan's nouveau riche impulse buyers.

Dubbed the IN-3000 artificial intelligence (AI) calculator, it has no keys—just a blank touch-sensitive slate where you write down the problem to be solved. Canon believes that will appeal especially to engineers, who like to see equations written out. But the company admits that a calculator with pre-programmed keys is far more useful to most people. The pad can also be used as a simple word processor, and it translates simple *katakana* characters into complicated *kanji* characters.

Where does the AI come in? Well, says a Canon engineer, that term might be a bit of an exaggeration—although the calculator is very clever at recognizing even sloppily written numbers. But don't look for the product to show up in U.S. stores. Japan's middle class, still adjusting to its newfound affluence, is an easy sell for expensive toys, says the engineer, "not like you Americans, who are much more pragmatic."

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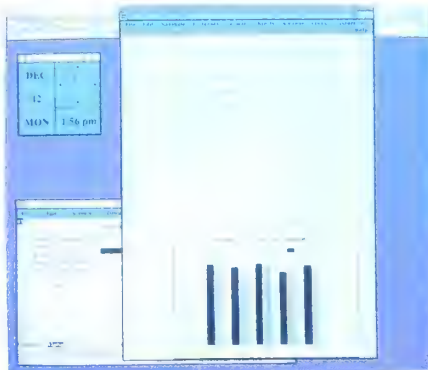
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THE WOLF AT THE DOOR DOESN'T LOOK SO SCARY

If 1990 brings a downturn, it may not be as ferocious as usual

The last recession was a killer. Unemployment jumped to 10.7%, interest rates were in the high teens, capital spending plunged, and the housing market crumbled. In the space of 15 months, real output shrank by 3.5%. The 1981-82 recession sent shock waves through the economy that reverberated for years.

Some economists are starting to wonder what the next recession will look like. Their curiosity may seem prema-

recession," says Allen Sinai, chief economist at Boston Co., who is expecting that in 1990 output will fall during two quarters—the number required for a downturn to qualify as a recession. And the next recession, when it comes, will also have some singular features. Certain sectors, for instance, may behave differently than in past recessions.

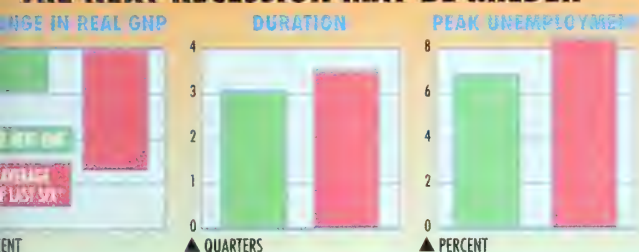
A mild recession starting at the end of the year would probably last no more than three quarters, says Stephen S.

But starts are unlikely to fall as far next time around—simply because they've been falling at a more gradual rate since 1986, when they averaged 2 million units. Housing starts are now averaging 1.5 million units a year.

Similarly, consumption, which accounts for about two-thirds of GNP, would probably slip by a modest one or two-tenths of a percentage point in a recession. Consumption stays relatively flat in recessions because purchases of basic goods and services cannot be easily deferred. But consumption had been growing at a heady 5% to 6% annual rate earlier in the expansion, and an abrupt stall could have shaved a couple of points off the GNP easily. Now, though, there may be less distance for consumption to fall. The rate of growth has moved steadily lower, and retail sales actually fell 0.4% in February.

But the biggest swing factor in moving from expansion to recession is the

THE NEXT RECESSION MAY BE MILD



NOT INCLUDE THE BRIEF RECESSION FOLLOWING THE IMPOSITION OF CREDIT CONTROLS IN MARCH, 1980

HOW SOME SECTORS MIGHT BE HIT



DATA: MORGAN STANLEY & CO. AVERAGES, BW ESTIMATES

ture—after all, the economy is in its seventh year of expansion and still humming, and the unemployment rate just hit a 15-year low of 5.1%. But that's exactly the problem. As more resources get used more intensely, economists expect the pressure on prices and wages to build. And as the Federal Reserve responds with higher interest rates, the economy will feel the pinch and head into a decline. So far this outcome has been averted. And slow growth without contraction may yet be achievable. But many economists insist that even the Fed's gradualist approach to fighting inflation will take its toll. "It's like loading one rock after another on a person's back," says Donald Ratajczak, director of economic forecasting at Georgia State University. "Eventually the cumulative weight will topple him."

So a recession, possibly beginning late this year or early next, is inevitable, say Ratajczak and others. But the good news, according to most economists, is that the next downturn will be mild—not nearly as wrenching as the ones in 1973-75 and 1981-82. "The Fed simply won't tighten enough to propel us into a deep

Roach, economist at Morgan Stanley & Co., and would shrink real output in that period by about 0.8%. That compares with a contraction of nearly 4% in the previous two deep downturns and an overall postwar average decline during recessions of 2.7% in real output (charts). A modest decline is in store, says Roach, because of what's been happening over the past year or so.

SLOWER REFLEXES. First of all, the Fed's gradualism has put it "ahead of the inflation curve," says Roach, so it shouldn't have to jack up rates abruptly to deal with the threat of rising prices. Furthermore, observes Mickey D. Levy, chief economist at First Fidelity Bancorp. in Philadelphia, inflation is only about half as high as it was before the last recession, while short-term interest rates are higher, after inflation, than they were in 1979-80, before the last recession.

That means a kind of restraint has already been imposed, keeping growth subdued in parts of the economy, such as housing, that usually take a dive in a recession. In steep recessions, housing starts can plunge by as much as 50%.

business sector, which, as sales plummet, must slash inventories, cut production, and shelve spending plans. In the past, during a deep recession, inventories plunged by as much as \$86 billion over a few quarters, while capital spending fell off by more than 10%. Together, these factors can account for two-thirds or more of the total decline in GNP. Next time around, however, business may not have to react quite so dramatically.

For one thing, executives have been loath to let inventories build for too long. Although there have been a couple of quarters of heavy inventory accumulation in this expansion, businesses have generally moved quickly to trim production schedules and correct imbalances. And on the capital spending front, companies may decide that competitive pressures require that they look for easier cuts somewhere else in their budgets (page 74).

IMPORT SLUMP. Foreign trade, too, is likely to play a stabilizing role. The widening trade deficit sapped U.S. growth in the early 1980s as imports outran exports. But during the next recession, the trade gap should narrow, because as to-

tal consumption slows down, consumption of imports—many of them discretionary items—should slow even more markedly. Exports, economists believe, will remain stable unless the U.S. recession is so deep that it becomes contagious and sharply cuts overseas demand for U.S. goods. Sinai estimates that a narrowing trade deficit, attributable to slowing imports, could add one-quarter

of a percentage point of growth in 1990.

Even private debt doesn't worry as many economists as it once did. "This time around," says Sinai, "household and corporate balance sheets aren't way out of line." If financial strains can be contained, that too would keep a mild recession from becoming a deeper one.

To be sure, not everyone believes that a recession—even a mild one—is neces-

sarily in the cards. Some, such as David Hale of Kemper Financial Services Inc., say the economy is in for a couple of years of stagflation, with inflation at 5% or more and real growth at only 2%. But if the next recession turns out to be a mild one, it will be the first time in 20 years that bad times have seemed so manageable.

By Karen Pennar in New York

THE FED'S BRAKES AREN'T SLOWING CAPITAL SPENDING

The 'animal spirits' of industrialists are strong," says Jerry J. Jasinowski, chief economist for the National Association of Manufacturers. "Businesses are more bullish on capital spending these days, no matter where they are in the business cycle." He's right, so far: After a rocky fourth quarter, nondefense orders for capital goods are rising again. Spending on plant and equipment is likely to grow by about 4.5% in 1989, adjusted for inflation—significantly faster than the real growth of 2.9% anticipated for the economy as a whole.

Businesses may soon demonstrate just how strong their animal spirits are. Faced with rising prices, the Federal Reserve Board has been pushing interest rates up to slow the economy. In the past, this was a signal for companies to stop investing. If they react the same way now, the economy could go into a deep recession instead of the mild slowdown that the Fed intended.

But this time executives may not be so quick to slash spending—even if rates climb another point or two. For one thing, corporations have a lot more ways to raise money than in the past. More important, executives fear they may lose market share to foreign competition if they don't keep investing in new capacity and better equipment. Even if a recession comes, says Carol B. Moerdyk, director of corporate planning for Boise Cascade Corp., "there's no urge to pull back."

PAPER PROFITS. Scarred by the competition that forced so many plant closings in the early 1980s, companies have shunned adding capacity since the expansion began in 1982. Instead, they bought computers and other high-tech equipment to cut costs. Now many industries are operating at close to 90% of capacity.

In response, companies are finally adding new facilities, even while continuing to modernize equipment. The

paper industry, at full capacity for years, is expected to boost capital spending by 28% in 1989. And certain companies are moving even faster: Boise Cascade will spend \$700 million this year, up from \$452 million in 1988. Moerdyk says about 60% of that \$700 million will go toward expanding production to keep up with the fast-growing market for coated and uncoated white papers.

The paper industry isn't the only big spender. In chemicals, the real rate of capital spending is expected to rise by 10% this year. And after a long bleak period, the big six steelmakers—USX,

stances to create a cash shortfall." Potlatch has roughly \$100 million in short-term investments and plans no further short-term borrowing, so rising short-term rates would boost earnings.

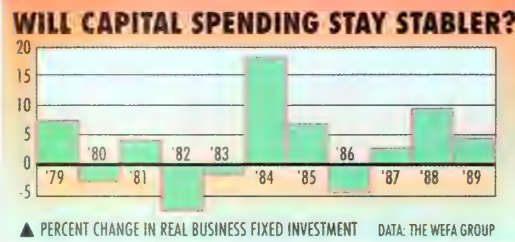
Big companies may be able to ride out rising rates, but what about smaller ones? In the past when credit was tight, notes R. Glenn Hubbard, an economist at Columbia Business School, small and medium-size companies had more trouble than their larger counterparts getting loans. "But since 1970 the capital markets have moved in the direction of fewer credit constraints," he says. A greater array of financing choices, from junk bonds to bank loans, is available to companies of all sizes.

But even if companies say they'll keep spending, their customers might not be able to. Sluggish sales are generally credited with having a greater impact on investment plans than rising rates. According to Edgar R. Fiedler of the Conference Board, the only reason people stop investing is "the feeling that it's not the right time."

COLD FEET? If it's not the right time stateside, though, it might be elsewhere. In 1970 exports accounted for 6.6% of GNP; now they're 11% and climbing. So a downturn in domestic demand doesn't necessarily mean companies should stop investing. "This is a factor you wouldn't have seen 10 years ago," says Richard E. Storatt, vice-president at the American Paper Institute.

Of course, even spendthrift companies may get cold feet if the economic outlook darkens. But competitive pressures are still bearing down on U.S. producers, and there may not be a second chance. "If businesses cut real capital spending by 15% like they did in the last two recessions," says Stephen S. Roach of Morgan Stanley & Co., "it's tantamount to industrial suicide."

By Michael J. Mandel in New York, with Jonathan B. Levine in San Francisco and bureau reports



Bethlehem, LTV, Inland, National, and Armco—are planning to boost capital spending in 1989 to \$2.1 billion, up 23% from 1988 and 117% from 1987. Most auto makers plan to keep spending, too, despite the recent slowing in sales. That includes Japanese auto makers operating in the U.S., which are spending heavily on plant and equipment and importing some of the capital goods they need (page 22).

Executives promise that even rising rates won't alter spending plans. Arco Chemical Co., for one, has no plans to cut its ambitious program, even if short-term rates climb. With worldwide demand rising for its main product, propylene oxide, Arco aims to double overall sales in five years. Papermaker Potlatch Corp.'s \$210 million capital budget for 1989 would be unaffected by rising interest rates. "Cash flow drives capital spending," says L. Pendleton Siegel, Potlatch's chief financial officer. "It would take extreme circum-

“... the chef's five-star blending of these familiar ingredients delivers a kind of harmony that is hard to find even if you are prepared to spend twice the money.”

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THE BOOM IN GOLF AS BABY BOOMERS HIT THE LINKS

They're jostling for tee time, and the industry is running just to keep up



THE U.S. MASTERS TOURNAMENT, AUGUSTA, GA.: IN FIVE YEARS THE PGA'S REVENUES FROM TELEVISION AND OTHER FEES HAVE ALMOST TRIPLED

Many golfers dream all week of teeing off first thing Saturday morning. But these days, realizing that dream is often a nightmare. During the season at Long Island's Bethpage State Park, players begin lining up shortly after midnight to secure an early tee time. In Los Angeles, it's even worse. Those who hope to play at Knollwood Golf Course in the San Fernando Valley on Saturday need to show up a week in advance. By 4 a.m. most Saturdays there's already a line of players waiting to reserve for the following week, and by 7 a.m., says pro John Wolgamott, "we're sold out."

Today golf is a \$20 billion industry in the U.S. with a growth rate that is nothing short of phenomenal. The National Golf Foundation estimates that 22 million people currently play golf, up 25% in two years. The foundation, which recent-

ly paid McKinsey & Co. to help draft a strategic plan for the sport, looks for spending on golf to hit \$40 billion within 10 years—if investors can find the land and the money for at least one new golf course a day over that time. But given the scarcity of land around the big cities, where golf courses are most needed, and construction costs that often top \$3 million, golfers are unlikely to see shorter lines any time soon. That's especially true in California and from Boston to New York, where space for golf courses is in short supply.

BETTER DIMPLES. What is becoming an increasingly nettlesome inconvenience for golfers, however, is likely to become a bonanza for companies selling golf equipment, managing golf courses, building resorts, or running marketing campaigns linked to the professional golf tour. To win a hefty share of

this burgeoning market, both in the U.S. and overseas, the race is on to see who can build the plushest resort, the most accurate golf club, and the longest-traveling ball. Wilson Sporting Goods Co. for example, recently hired an aeronautical engineer from Boeing Co. to help design the dimples on a golf ball in order to improve performance in the wind.

Best of all, as far as the companies are concerned, golf caters to the kind of people business loves best: upscale consumers. Golf is the only major adult sport where participants play and spend more as they age. Just the initial investment in equipment costs a typical golfer \$400 to \$600, for example, compared with \$150 or less for a tennis player. And as baby boomers grow wealthier and older, golf is just the ticket. "The baby boomers have played ten-

s and racquetball and done their marathons, but now their bodies are wearing out," says Shelby Futch, director of John Jacobs' Practical Golf Schools, where enrollment has doubled to 6,000 since 1986.

Golf is also growing more popular because it is a sport where the long rides and walks between strokes afford plenty of opportunity to do business. At the Jack Nicklaus Academy of Golf at Grand Cypress Resort in Orlando, where students pay \$1,800 for three days of lodging and lessons, school Director Fred Griffin says much of the growth in interest comes from people eager to get their games up to respectable levels for business contacts. A growing proportion of such new players are women. Take the case of Sue Hilton, a manager with General Financial Systems. She works with car dealers, 90% of whom play golf, she says. Now she conducts much of her business on the course. "It's given me five hours with clients I never would have had before," she says.

BIGGER PURSES. Growing participation has helped professional golf become one of the greatest success stories in spectator sports. In the past five years the PGA Tour's total revenues from television, tournament operations, licensing, and real estate have almost tripled, to \$28 million, and the purses paid to players have doubled, to \$57 million in 1988. The Senior Tour for professional golfers over 50, which had only two events and a purse of \$250,000 in 1980, has parlayed the allure of Arnold Palmer, Chi Chi Rodriguez, and others into a 10-event circuit with a \$14 million annual purse.

Corporate America is fueling much of this growth. Sponsors such as General Motors, AT&T, Federal Express, and Neslé routinely pay up to \$3.5 million or more to have their names associated with the tournaments. Other companies provide hospitality tents or rent chalets where their clients can socialize with the professional golfers. In the pro-am day before each main match on the tour, executives pay up to \$6,000 just to play 18 holes with one of the stars, with the proceeds going to charity. Because audiences who watch golf on TV or who come out to the tournaments are far above average in income and education, golf also is an excellent vehicle for target marketing to the affluent.

The golf boom holds even more promise for companies serving the growing army of recreational golfers, whose spending dwarfs that connected with the PGA Tour. The early winners have been golf resorts. The golf foundation figures 7 million golfers took a



golf trip last year and spent a total of \$7.8 billion on travel and lodging. "There's no question that golf has raised our occupancy levels," says Roger Maxwell, vice-president of golf operations for Marriott Corp., the largest golf resort operator. Marriott studies show 95% of the corporate groups coming to resorts would have gone elsewhere if golf were not available. At Hyatt, which has 10 hotels that are part of or adjacent to golf courses, "we have changed our thinking with regard to our whole resort expansion program," says President Darryl Hartley-Leonard. "We simply would not build a resort without golf today."

DESIGNER COURSES. At the top resorts, price seems to be almost irrelevant. Although it now costs \$150 for a member of the public to play 18 holes at Pebble Beach on California's Monterey Peninsula, the course is sold out a year in advance during the peak autumn season. The price will soon be raised to \$163.

Similarly, Landmark Land Co., an

American Stock Exchange company that has opened eight courses in three years, charges \$150 to play the PGA West Stadium Course in La Quinta, Calif. The course, which hosts the Skins Game, a widely watched TV contest in which four prominent golfers compete, is among the toughest on the tour, but it still turns away plenty of recreational golfers during the heavily booked winter season. Like 70% of the golf courses being built today, PGA West is also part of a real estate development. Landmark bought the land for \$15,000 an acre in the early 1980s. After the Stadium Course opened, residential lots surrounding the course soared to \$140,000 an acre.

Some of the plushiest golf attractions are in Hawaii. Waikoloa Land Co., partially owned by the Bass family, already has two courses designed by Robert Trent Jones Jr. and is now spending \$16 million to add a course designed by Tom Weiskopf in Waikoloa on the island of Hawaii. One reason for the high cost is the necessity to crush the surface layer of lava,

THE \$20 BILLION GOLF INDUSTRY...

FEES
AND OTHER GOLF
COURSE OPERATIONS
\$2.1

EQUIPMENT
\$5.7

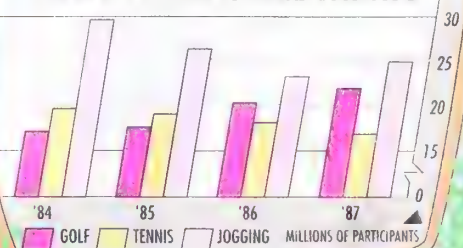
TRAVEL
AND RESORT LODGING
\$7.8

TOURNAMENT ADMISSIONS
AND SPONSORSHIPS
\$0.3

SECOND HOMES IN
GOLF DEVELOPMENTS
\$3.8

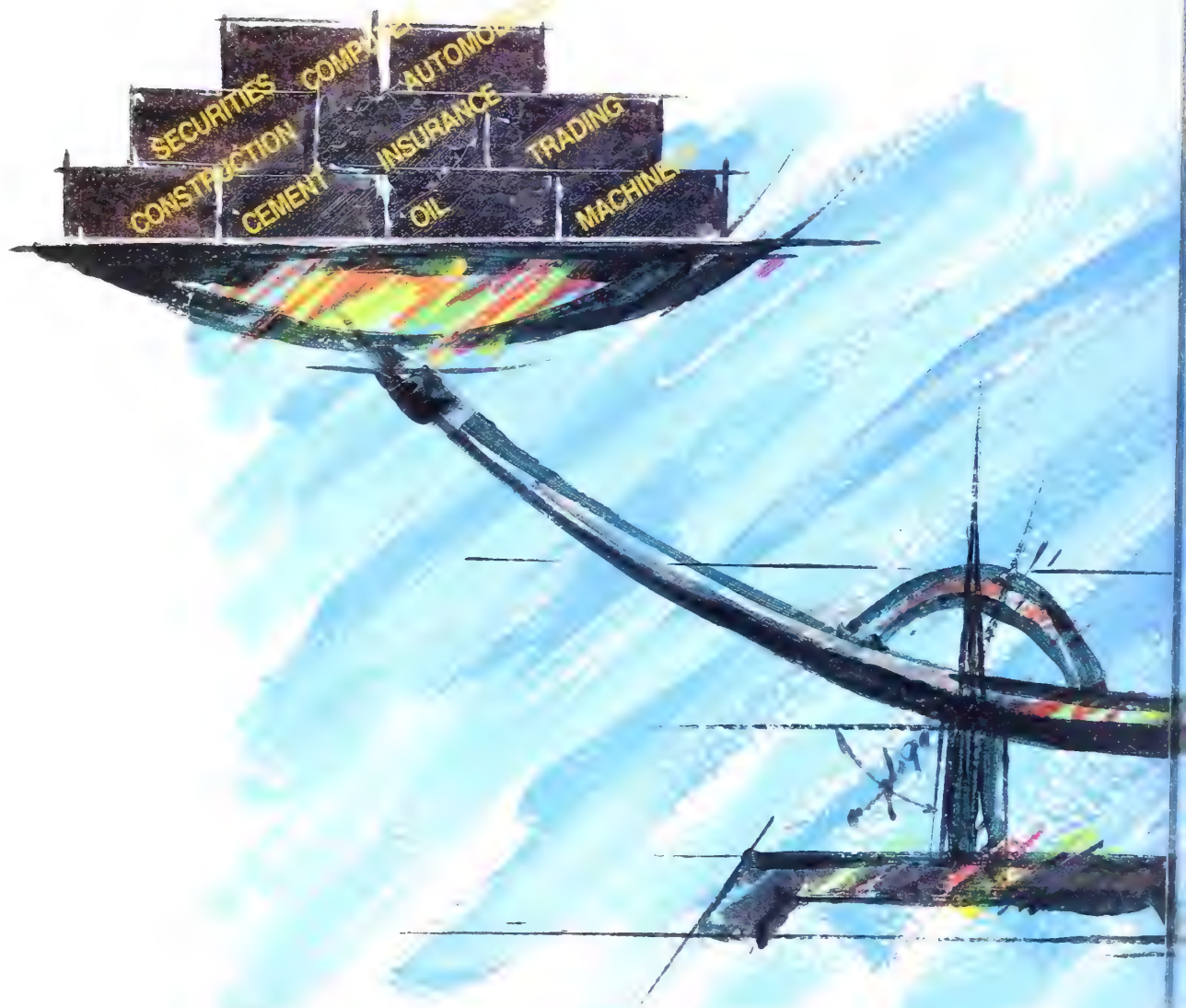
ALL FIGURES IN BILLIONS OF DOLLARS

...IS GROWING, WHILE MORE ACTIVE SPORTS ARE FADING



DATA: NATIONAL GOLF FOUNDATION, MCKINSEY & CO., NATIONAL SPORTING GOODS ASSN

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Sports Business

remove it, and then truck in topsoil. At the Hyatt Regency Waikoloa, golf is an integral part of what may well be one of the most luxurious resort hotels in the world. After golf you can join the dolphins in a man-made lagoon.

In the \$2.1 billion-a-year U.S. market for golf equipment and clothing, the competition is taking on a decidedly foreign accent. Amer Group Ltd., a conglomerate based in Finland, which acquired control of MacGregor Golf Co. at the beginning of 1987, has now agreed to purchase Wilson for \$200 million, plus the assumption of \$190 million of outstanding debt. The acquisition will make Amer one of the top players in the U.S. golf-equipment business.

IRONS IN THE FIRE. The companies that benefit from the game's bright future are likely to be the ones that can get an edge in technology. One of the oldest names in sports, Spalding Sports Worldwide, is now owned by the wealthy Cisneros family of Venezuela. Spalding sells \$200 million worth of golf balls a year and \$100 million of other golf equipment. After extensive research and development, Spalding has introduced the Top-Flite XL II, which has an improved core and better aerodynamics.

THE CHANGING GOLFER

	1986	1987
INCOME*	\$85.5M	\$42.1M
AGE*	34.7	37.9
SEX	77% male	77% male
INCOME RANGE	34%	41%
EDUCATION		
FIVE YEAR*	75	19
PERCENT		

One of the more controversial items of golf equipment is the Ping Eye2 set of irons made by privately held Karsten Manufacturing Corp. The irons, costing up to \$850 for a full set, feature square-shaped grooves instead of the traditional V-shape. Although these clubs are very popular among recreational players, the PGA Tour recently announced that it was banning these and all other similar clubs from the tour starting next year. The reason: Players using the Ping irons have an unfair advantage.

Yet another marketing breakthrough has been scored by Taylor Made Golf

Co., which introduced drivers and other "woods" made out of metal in the early 1980s. When golfers became convinced these metal woods gave them more distance and accuracy, sales exploded. They rose 300%, to \$76 million, in the fiscal year ended last Oct. 1, and are expected to reach \$130 million this year.

LINK LEISURE. Some bigger U.S. companies are stepping up their efforts, too. American Brands Inc., the \$12 billion consumer-products company, generates nearly \$300 million in sales annually from Titleist and Foot Joy brands sold by its Acushnet Co. subsidiary. Acushnet participates in all four basic golf gear markets: balls, clubs, gloves, and shoes. It claims to be No. 1 in sales of premium balls, gloves, and shoes sold in pro shops but only fourth in clubs. The company is now building a plant to open in late 1990, alongside its existing plant in New Bedford, Mass., that will increase its capacity 25% and enable it to produce two-piece golf balls. Says John T. Ludes, president of Acushnet and a group vice-president at American Brands: "We feel we will be in a position to compete with anything the Japanese or Europeans might come up with."

Ludes is feeling the heat from foreign

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WANT TO SET UP YOUR OWN TELEMARKETING OPERATION BUT AREN'T SURE WHAT YOU NEED TO BEGIN?

competitors because golf's growing popularity is a global phenomenon. In Europe, interest is especially strong in Sweden, West Germany, and Britain, golf's ancestral home, where officials at the English Golf Union say 500,000 golfers cannot join clubs due to lack of space.

France expects to have 90 public courses by 1990, up from only one in 1980, thanks largely to subsidies championed by President François Mitterrand, who is a golfer.

UNIMAGINABLE HEIGHTS. No other nation in the world comes close to the golf fanaticism displayed by the Japanese, however. Although golf has long been an integral part of Japanese business life, interest is now surging because of increasing affluence and the growing prevalence of the five-day workweek. The number of rounds played at Japan's crowded courses has increased 50% since 1979, and officials are expecting the number of golfers to jump 23%, to 16 million, by 1991.

Because there are nowhere near enough courses to handle all this de-

mand, the price of playing golf soared to heights unimaginable in any other part of the world. Since 1982 the price of a membership in eastern Japan has jumped more than 400%. It now costs \$2.4 million to buy a membership in the exclusive Koganei Country Club, prized



A TOKYO DRIVING RANGE: CLUB MEMBERSHIPS CAN COST A FORTUNE

because it is only 30 minutes from Tokyo's western suburbs.

This means that playing golf can be a burden even for well-off Japanese executives. Yoshikazu Kiyoto, manager of foreign bond trading at Nikko Securities Co., paid \$87,000 to join the Seve-

Ballesteros Golf Club outside Tokyo six months ago. To play on weekends he must reserve a tee time three weeks in advance. Once there he pays \$79 in greens fees and \$236 for each guest. During the week, Kiyoto's only outlets are Tokyo's huge, multistoried driving ranges. But demand is so great there is usually a line—summer and winter.

Could Japan be a vision of the future for American duffers? With land in far greater supply, it's not likely that golf mania American-style will reach Japanese proportions soon. That is small consolation, however, to the golfers trying to get into such prestigious clubs as the Winged Foot Country Club in the New York City suburb of Mamaroneck. The country club's fathers recently stopped taking new ap-

plications when they figured out that their current waiting list is so long that new applicants might have to wait 10 years.

By William C. Symonds in Orlando, with Brenton Welling in New York and bureau reports

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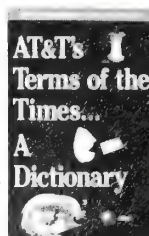
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IS YOUR COMPANY TOO BIG?

"For every type of animal there is a most convenient size, and a large change in size inevitably carries with it a change of form... just as there is a best size for every animal, so the same is true for every human institution."

—British scientist J. B. S. Haldane, 1928

One chilly winter day in 1987, Leslie H. Wexner was driving his car up the road to The Limited Inc.'s huge warehouse and headquarters in Columbus, Ohio. Wexner, founder and chairman of the retail clothing chain, was beginning to fret about his organization's agility.

With revenues approaching \$4 billion, The Limited no longer was the small, fleet competitor that set the pace for specialty retailing for a decade. Profit margins were slipping. The company's distribution system was showing signs of strain. Was The Limited becoming too big to manage? As Wexner would say at a series of meetings over the next few weeks: "The Limited is beginning to look like General Motors. Do we act like them?"

Wexner was asking a question that is on the minds of lots of leading academics and executives these days. Are huge, sprawling corporations the dinosaurs of our economy? Are smaller, more nimble organizations our economy's salvation?

GURUS VS. GIANTS. Big vs. Small has become one big debate—and small seems to be winning. Scores of management gurus and thinkers such as consultant Thomas J. Peters (*In Search of Excellence*) and commentator George Gilder (*The Spirit of Enterprise*) are on the lecture circuit, vilifying the inefficiencies of Big Business. And for good reason.

Small companies have emerged as the engine of the American economy, fueling much of the job creation and technological innovation in the U. S. They have generated a great majority of the more than 20 million new jobs added to the economy since 1977, according to Massachusetts Institute of Technology econo-

HOW COMPANIES

BIG

- Sprawling plants
- Vertical integration
- Economies of scale
- Hierarchical organization
- Organization men
- Grabbing market share
- Mass marketing
- Quantity



E TYPICALLY RUN

SMALL

Small factories
Subcontracting
Flexibility
Joint organizations
Entrepreneurs
Finding new markets
Niche marketing
Quality



mist David Birch. Entrepreneurs, including many who are corporate escapees disenchanted with the plodding pace of big-company life, say that Big Business has failed to pioneer most of the decade's most important technological innovations.

"Virtually every innovation in computation since the mainframe—the microprocessor, personal computer, minicomputer, workstation, supercomputer, and much software—has been started or commercialized by venture-backed, entrepreneurial companies," says Benjamin Rosen, a leading venture capitalist. "They've created millions of jobs. It's what has kept us alive in world competition."

Years ago, when foreign businessmen visited the U.S., they gravitated to Detroit and Pittsburgh to witness what was right about the American economy. Today they trek to Silicon Valley and Route 128. The fact is, large American corporations have failed to maintain the nation's leadership in key industries from consumer electronics to steel. Indeed, a way to virtually guarantee that a company will not lead its industry in profitability is for it to lead in size. The biggest companies are the most profitable—on the basis of return-on-equity—in only 4 out of 67 industries in the BUSINESS WEEK Top 1000. Well over half the time, the biggest corporate player fails to attain even the industry average return on invested capital.

"Size has become a paramount issue, and somewhat smaller is apparently becoming much more beautiful everywhere," says Peters. In a fast-changing world, management flexibility may well be far more critical than all that 1950s talk about how massive scale provides certain economies in research, production, marketing, and sales. Birmingham Steel Corp. can produce a ton of steel with only a third of the labor of the big steelmakers. And Compaq Computer Corp., notes Peters, can develop a new computer three to five times faster than IBM.

SIGH OF RELIEF. At The Limited, Wexner appears to have solved his concerns about bigness with a major overhaul. Since early 1988, he decentralized the company along divisional lines, put more authority in the hands of lower-level managers, and gave stores face-lifts. Sales, margins, and, recently, profits have picked up. If Wexner was indeed worried that his company was becoming too big, he can now breathe a sigh of relief—at least until his company gets bigger still.

Even as they argue that size is necessary to compete against global rivals, executives at many big companies are trying to mimic smaller firms. One corporate Goliath after another is trying to act like the Davids of the business world, creating smaller, highly decentralized business units and giving managers greater flexibility and freedom with less staff review. General Electric Co. Chairman Jack F. Welch now speaks of transforming GE into a "big-company/small-company hybrid," combining the large corporation's resources and reach with the small company's simplicity and agility. "We want the best of both... a big company with the heart and hunger of a small one," he says.

To accomplish such aims, he and other corporate leaders are hacking away at bureaucracy by axing management layers, pushing down decision-making, and shortcutting the approval process. American Telephone & Telegraph Co. is among the latest to announce a massive reorganization to quicken the pace of operations and make its culture more entrepreneurial. Not surprisingly, some of the most successful big companies, from Johnson & Johnson to Hewlett-Packard Co., are those that have organized themselves into groups of smaller companies.

Why? Because despite the bigger-is-better notion propagated by some investment bankers and takeover attorneys, the global marketplace requires attributes seldom associated with bigness. "It's demanding speed, agility, the ability to improvise and customize," says Ervin R. Shames, chief executive of General Foods Corp. "Those are tactics and behavior normally associated with the little guys, not the big ones." Of course, not everyone buys

the idea that small is beautiful. Big companies marshal plenty of ammunition on their side, too. The 500 largest corporations alone account for nearly 30% of U.S. gross national product, and they employ 80% of the scientists and engineers who work in industry. "Only big U.S. companies can amass the resources required to compete with foreign enterprises that are often gigantic and subsidized or even owned by the state," says Pat Choate, vice-president of TRW Inc.'s office of policy analysis. Such thinking has led to major consolidation in dozens of industries, from appliances to tires to airlines to en-

tertainment. It informed the merger deal in early March between Time Inc. and Warner Communications Inc.

'HUMBUG.' Other proponents of megacorporations go even further. Charles H. Ferguson, a former IBM analyst who is a scholar at Massachusetts Institute of Technology, says "humbug" to most of the arguments for smaller companies. If the U.S. is to withstand increasing foreign competition, Ferguson maintains, it will have to rely on the big corporation and on government support of such strategic industries as semiconductors and computers. Entrepreneurs—particularly

in high technology—only distract and divert the efforts of the corporate giants, he believes.

"Small companies can't survive against Japan's stable, concentrated, and protected alliances," says Ferguson. "Most of these startups disappear after the first five years. I forecast a short life span for Compaq. It will either disappear or come a Japanese or Korean company to give them two to five years."

Many management experts see a vastly changed world economy in which the attributes of size—access to greater resources, economies of scale, and sta-

THE GOLIATHS MEET THE DAVIDS: BIG-COMPANY

'Sure, large firms have been screwing up in a massive way. But funding startups is not our salvation'

—Charles H. Ferguson
Researcher, MIT



His critics call him a modern-day Chicken Little whose sky-is-falling pitch is little more than nonsense. But Charles H. Ferguson, a 33-year-old Massachusetts Institute of Technology scholar, is gaining much attention for his beliefs on how the U.S. should compete against Japan. His prescriptions, which include government support for strategic industries—rankles the entrepreneurial community, because Ferguson believes that startups have some cases weakened our ability to compete.

"These firms shoot up like meteors for five years and then fall down to earth," he says. "This fragmentation and instability is not a sign of well-being. Sure, large firms have been screwing up in a massive way. But funding startups is not our salvation. You need large firms or collectives of firms that cooperate efficiently against the Japanese." Most startups, he thinks, pay scant attention either to employee development or to long-term relationships with suppliers and customers—hallmarks of Japanese management. "In Silicon Valley, the career plan for employees amounts to a bonus at Christmas."

As chairman of one of the world's largest companies, Roger B. Smith of General Motors Corp. might be expected to wax eloquent on the virtues of bigness. But with all the trouble GM has had lately, Smith isn't as outspoken an advocate of sheer size as you'd expect.

"Being big doesn't guarantee that you're going to be good," he says. "Today you need to foster an entrepreneurial spirit. You've always got to go back and check and say: 'What's my main purpose here in life?' Saturn [GM's effort to take a new approach in building small cars] is a good example of how a large-size company can be a small company in an innovative way. There are lots of ways to do it. But just because you're small doesn't give you a license to succeed. Bigness doesn't keep you from failing." Still, Smith agrees it's particularly tough for a big corporation to attract innovators and entrepreneurs: "It's not easy to develop and sustain them in a large, established organization. Where are all the hotshots right now? They're in Microsoft and other things where individual people can [innovate on their own]."

'Just because you're small doesn't give you a license to succeed'

—Roger Smith
Chairman, General Motors Corp.



'If the so-called dinosaurs are going to be extinct, why would anyone invest in them?'

—Theodore Levitt
Editor, Harvard Business Review



Theodore Levitt doesn't want to be thought of as an apologist for Big Business. But the well-known Harvard business school professor is one of the people who have gone too far in their attack on the efficiency of the large corporation.

"Some things can only be done by large organizations," he says. "The question is going to be the general contractor to go to the moon or to build a massive pipeline in Alaska? If you had to commit money for a project that takes 10 years to complete, like building a plant, would you turn it over to a small company? Some things inherently require scale." Besides, he notes, large companies tend to be far more stable than smaller ones. "Where would you prefer your pension fund invest? General Electric, IBM, and Philip Morris? Widget Semiconductor Corp. and some new hamburger establishment? The obvious answer says something important about the stability of large corporations. If the so-called dinosaurs are going to be extinct, why would anyone invest in them?"

—are not nearly as crucial as the flexibility and agility to compete in fast-changing markets. In this world, mass production and its demand for huge investments in highly specialized equipment giving way to flexible manufacturing teams, smaller production runs, and new marketing. Management concepts of the past—vertical integration, huge sprawling plants, mass production, and fixed careers—are being supplanted by new ideas (table, page 84).

We've always had small companies fighting chunks out of big companies' sales," says Peters. "What is new is that the thorns in big corporate sides have grown up to be big companies that have

nothing to do with the GES, GMS, IBMs and Seares of the world. GM grew up when you were supposed to have a tall hierarchy and you were supposed to be vertically integrated. The relative good news is that the new breed of cat—Wal-Mart, Federal Express, MCI Communications, and Apple Computer—grew up in a new environment and didn't develop those habits from the start."

NO BAD THING. The current debate is hardly new. The emergence of the trusts in oil, tobacco, whiskey, and other industries in the late 1800s led to the first antitrust laws. And for years economists have probed the strengths and weaknesses of size, often justified by the catch-all phrase

"economies of scale." Yet despite concerns over monopolistic practices by larger enterprises, bigness wasn't thought to be such a bad thing.

In 1942 the world-famous economist Joseph A. Schumpeter credited large companies with most of the progress in business. "The modern standard of life of the masses evolved during the period of relatively unfettered 'Big Business,'" he said. "Big Business may have had more to do with creating that standard of life than keeping it down."

Since the late 1940s, every Economics 101 student would have learned from Paul A. Samuelson's text that "large size breeds success, and success further suc-

GE VS. ENTREPRENEURIAL AGILITY?



computer
try is
whelmingly
l, but it's
because of
George Gilder

Author of seven books, George Gilder, 49, is both a student of the electronics industry and a controversial thinker. Four years ago he sang the praises of the entrepreneur in *The Spirit of Enterprise*. Gilder helped ignite the current Big-vs.-Small debate with a *Harvard Business Review* article last year.

Put simply, he disagrees vehemently with recent critics of entrepreneurship. Smaller companies, he says, have been the economy's salvation. "Our computer industry is overwhelmingly No. 1, but it's not because of IBM," he says. "The main reason for our dominance is the hundreds of computer and software companies that have been growing five or six times faster than IBM for the last 10 years. The belief that Japan's huge corporations and government involvement is behind its success is flawed. General Electric is bigger than Hitachi, and GE has the resources to sustain a large research-and-development activity. Instead, it chose to withdraw from televisions and semiconductors. Our large companies haven't maintained our competitiveness."

founder and head of fast-growing Cypress Semiconductor Corp., T. J. Rodgers is the prototype of the Silicon Valley entrepreneur. He's a brilliant technologist with novel ideas about how a company should be run.

Gilder, 41, thinks it "scary" that entrepreneurialism even needs to be led. "Large companies do not bring new technologies and products to marketplace very efficiently," he says. "And I can't think of a worse capitalist than the chief financial officer of a \$1 billion company." Peters believes the U.S. has consistently overcome its larger, Japanese in computers and semiconductors through quickness and technology, not mass. One major reason: Big organizations spend too much time arguing why they shouldn't do something rather than working to meet a goal or objective. "The big guys will always tell you how it's impossible to take the hill," he says. "Small companies look at the challenge, figure out how to take the hill and to limit the casualties, and then attack it."

'Large companies do not bring new technologies and products to the marketplace very efficiently'

—T. J. Rodgers
President, Cypress Semiconductor



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Thomas J. Peters

Thomas J. Peters made his fame and fortune as a management guru by extolling the virtues of successful big American companies in his 1982 book *In Search of Excellence*. In more recent years, however, Peters has become a great fan of the entrepreneur and a frequent critic of big-company lethargy.

"When things get very big, they tend to get very sluggish," he says. "The only real card the U.S. holds in global competition is the combination of our entrepreneurs and our financial markets. Our strength is The Limited, Nordstrom, and Wal-Mart knocking off J. C. Penney and Sears. Our strength is an Apple, Compaq, or Cray giving IBM fits. It looks messy, but it's what keeps us in the game. The only reason Ford and General Motors are getting better is because pipsqueaks like Honda scared the pee out of them. There are two forces that drive out cholesterol in the big companies: our small domestic entrepreneurs and international competition. I think the former is doing a better job than the latter today."

A NICHE PAPERMAKER UNDERCUTS A GIANT



	Revenues	Employees	Three-year avg. annual ROE	Three-year avg. sales growth
INTERNATIONAL PAPER	\$7.8 billion	45,500	6.5%	18.1%
P.H. GLATFELTER	\$424 million	3,490	20.3	10.9

DATA: S&P PC COMPUSTAT PLUS

Talk about contrasts. Industry giant International Paper Co. is coming off the best year in its history. Riding the crest of a cyclical wave in the paper business, IP's net income soared 89%, to a record \$754 million on \$9.5 billion in sales last year.

But then there's little P.H. Glatfelter Co. in Spring Grove, Pa. Its enviable profit margin of 14.2% is nearly

double that of its much-larger Purchase (N.Y.) competitor—even given IP's record performance last year. Over the past five years, Glatfelter's return on equity has averaged three times as high as IP's.

What's the difference? Start with management continuity. Chairman Thomas C. Norris is the first non-Glatfelter in the job and only the compa-

ny's fifth chairman in 125 years. His counterpart at IP, John A. Georges, is the fifth executive to lead the company since the early 1970s—and the fourth recruited from outside the industry.

Consider the difference in employee relations. Norris likes to boast that he knows the names of most of his 1,250 employees in Pennsylvania and a good chunk of the 2,250 others outside the state. The same could hardly be said of Georges, whose company suffered a bitter, 16-month strike that ended last October.

Then look at markets: IP's massive size brings with it massive exposure to the ups and downs of the paper industry as well as its less profitable commodity products. Glatfelter, like many smaller companies, is a niche player. Paper from its mills helps publicize stock in Wall Street prospectuses, preach religion in Watchtower Bible & Tract Society publications, and sheath tobacco in cigarettes. By nosing into such corners, it can run circles around companies 16 times as big. "We've picked and chosen the markets we can service best, and we service the hell out of them," says Norris.

cess. The statistical evidence on profits suggests that profits increase with size.... The most celebrated professional manager in history, General Motors Corp.'s Alfred P. Sloan Jr., conceded the difficulties of managing a large corporation, but he argued that growing big was critical to a company's success. "Growth, or striving for it, I believe, is essential to the good health of an enterprise," he said. "Deliberately to stop growing is to suffocate."

Besides, America has long been obsessively devoted to size and scale. For decades, the dream of virtually every American businessman was to drive his company to a level of sales that would land it among the biggest 500 companies—not to make the best products or most profits. Walter Adams, professor of economics at Michigan State University, credits much of that dream to pure ego. "If you command a platoon,

you're a second lieutenant," he says. "If you command a company, you're a captain. A division is worth a two-star general. The larger your command, the more pips on your epaulets. Obviously, with that goes prestige, power, perks, and pay."

So successful was GM that it became

the model for the postwar corporation. In his landmark book, *Concept of the Corporation*, management guru Peter S. Drucker held up GM as the definitive successful large organization. In recent years, however, Drucker has said that large institutions such as GM and ITT Corp. have basically outlived their useful-

ness. "A penalty of size is that you try to do everything, and no one can do everything well," says Drucker. He believes that most of the recent growth and innovation in U.S. business sprang from midsize companies that employ 200 to 4,000 people.

WILD FRENZY. Why the change of heart? Many critics of scale point to the conglomerate era of the 1960s and 1970s when bigness seemed to have less and less to do with either innovation or efficiency. In this wild feeding frenzy, ITT alone acquired some 200 companies, only to run the biggest fire sale in histo-

WHEN BIG COMPANIES TRY TO ACT SMALL

AT&T Chopping up six major businesses into 19 or more smaller groups. Goals: eliminate turf wars, deemphasize management by committee, encourage individual risk-taking, improve focus on individual markets

GENERAL ELECTRIC Chairman Jack Welch attacks "big company encumbrances" by cutting management layers between factory floor to executive suite from nine to as few as four. Staff should be "facilitator, adviser, and partner," not "monitors, checkers, kibitzers, approvers"

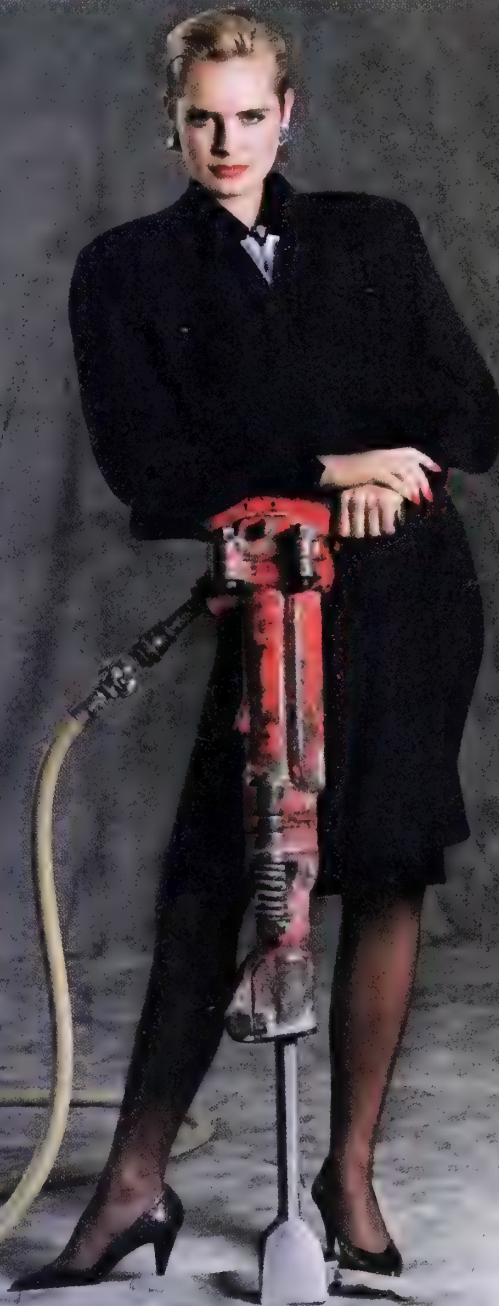
GENERAL MOTORS Chairman Roger Smith vows to dismantle entrenched bureaucracies by stripping out layers of management; seeks ideas from customers and suppliers; develops technological advances through acquisitions

HEWLETT-PACKARD To give managers "self-direction and ownership." President John Young divvies up the company's businesses into 50 units with own profit-loss, planning, and support responsibilities

MCDONALD'S Building on structure as far-flung collection of independent entrepreneurs; boasts a vice-president for individuality to "make the company feel small" through incentives and awards; autonomous franchisees credited with such innovations as McD.L.T. and Egg McMuffin

DATA: BW

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	Revenues	Employees	Three-year avg. annual ROE	Three-year avg. sales growth
WAL-MART STORES	\$15.9 billion	183,000	26.9%	35.6%
JAMESWAY	\$701 million	9,400	11.3	13.8

DATA S&P PC COMPUSTAT PLUS

Sam Walton and Herb Fisher go way back: 27 years to be exact. That's when Sam clipped the ribbon outside his first Wal-Mart in Rogers, Ark., and Herb opened up the doors of his first Jamesway discount store in New York state.

Both founder-chairmen sport no-frills headquarters, call employees by the more dignified term of "associates," and promote the same "we care" mottoes in stores. Over the years they have even borrowed a few merchandising concepts from each other.

But they part company rather quickly when it comes to growth and profits: Wal-Mart Stores Inc. is 26 times the size of Jamesway Corp., yet it still racks up profit margins three times as high as its smaller rival. Each square foot of Walton's stores generates \$210 of sales, nearly twice as much as Jamesway. So much for the agility of the smaller concern.

None of this seems to bother Fisher, 67, who concedes he also has lost to Walton, 71, a few times on the tennis court. "Sam's a brilliant merchandis-

er," he says. The way Fisher sees it, at least Jamesway has survived. "There are probably 50 other companies that aren't around anymore."

Wal-Mart, he concedes, has used scale to great advantage. Store managers are trained at the Walton Institute. A private, six-channel satellite-television network gathers store data, handles credit-card approval, and beams company news directly to employees. To keep tabs on sales and inventories, Wal-Mart also pioneered the use of Universal Product Code (UPC) scanning technology at the cash register. Jamesway is only getting around to outfitting two of its 121 stores with UPC scanners on a pilot basis this year.

But plain hard work may be the Walton edge. Senior executives spend five days a week visiting stores. Saturdays are spent repositioning merchandise based on mounds of computer research. It's not for everyone: In February, Vice-Chairman Albert L. Johnson, 53, resigned after only a year on the job. "He just burnt out," says a Walton associate. "Sam doesn't let up."

ry in the 1980s. The failure of America's huge corporations to meet fierce competition from abroad in steel, textiles, automobiles, and consumer electronics helped fuel the debate.

And the spectacular rise of the entrepreneur as an American folk hero raised the question: Would our economy be better off if it were composed of only smaller to midsize companies? One person likely to answer in the affirmative is T.J. Rodgers, founder of Cypress Semiconductor Corp., who is typical of the newest generation of entrepreneurs. Rodgers has built

a \$135 million company in five years by developing superfast memory chips for niche applications. He makes no secret of his desire to build Cypress into the biggest semiconductor maker. But he has different ideas of how to manage that growth: by establishing separate companies with their own chief executives and boards of directors to pursue related high-tech ventures.

"At about \$50 million in revenues, I felt I could run it," he says. "I could name everybody in the company. But as it grew larger, I found myself stretched. One Fri-

day night at 11 p.m., I realized that there wasn't a change, I'd have to stop sleeping within six months to keep up the pace." Rodgers split the company into divisions, only to discover that things were getting even more out of hand. At a stormy management meeting in 1986, he sat incredulous as chip designers argued with manufacturing managers over who was at fault for some quality problems. "All this political infighting scared the living hell out of me," says Rodgers.

His solution was to think up ways to regain the sense of camaraderie and the penny-pinching focus of a startup. He had already committed to building a second wafer-fabrication plant, but now he wanted to establish it as a separate entity—even telling his anointed chief: "If you work, I'll make you a millionaire." The plant was up and running in record time, producing \$400,000 in revenue within 18 months of its ground breaking in 1987. Typically, it takes a new plant two years to record significant sales.

'DREAMWORLD.' Not surprisingly, MIT's Ferguson pooh-poohs Cypress as just another entrepreneurial meteor likely to crash to earth. "Rodgers can remain small and unimportant company," he says. "But if he wants to grow, he'll have to go into a core market and run up against the Japanese. Then, he'll discover reality. Right now, he's in a little dream world."

Ferguson thinks it will take the might of a big company or a coordinated group of smaller ones to fight off the giants of Japan. Cypress and many other similar high-tech companies, believes Ferguson, only divert resources and talent from truly productive enterprises. In other words, small, in technology, is hardly good. Big, strong, and powerful is America's only hope to combat tough, new, global competitors.

What many executives are finding, however, is that it's less a question of managing size than of managing complexity. Those who flatly argue against size miss the point: Bigness still confers major advantages on some industries. Those who believe that entrepreneurs are weakening the nation's ability to compete against more organized foreign competition forget how crucial those upstarts are in keeping big companies competitive.

Both small and big rely on each other to make an economy strong. Big Business is often the principal customer of small enterprise. "To me, small is good, and big is good, and having the two of them is ever better," says Alexander MacLachlan, senior vice-president for technology at Du Pont Co. "The great strength of the U.S. is the combination."

It's true that today the principal concern of managers in large organizations is



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how to gain the advantages of smaller, nimbler companies. At the same time, the managements of smaller companies tend to be preoccupied with growing bigger, thereby gaining greater resources and wider distribution. "Both small and big companies are seriously engaged at having things the other one already has," notes Theodore Levitt, a Harvard business school professor.

That's why large corporations—from AT&T to Eastman Kodak Co.—are downsizing, spinning off unrelated businesses, and pushing down more authority in the organization. They want big company managers to act small. After all, many of the most successful big companies already boast these attributes. Johnson & Johnson with its 166 autonomous companies is one example. Another is Hewlett-Packard with its 50 independent business units, each with its own profit-and-loss responsibility and separate planning and support functions. The idea has always been to give managers enough "self-direction and ownership" in their businesses, says HP President John A. Young.

A recent study by consultants A. T.

Kearney Inc. found that only 12 of the top 200 industrial corporations have sustained 18 consecutive years' of financial success. What factors separated these firms—including Coca-Cola, 3M, Emerson Electric, and Heinz—from the pack? They think small and successfully manage complexity. "Their organizations are decentralized

To retain agility and limit complexity, many executives have abandoned the idea that self-sufficiency is a virtue

and lean," says Kearney's Robert W. Gunn. On average, they have only seven corporate staffers per 1,000 employees. Profit-and-loss responsibility is pushed down three or four levels below the CEO, rather than one or two. Managers have authority levels ranging up to \$20 million—10 times higher than in the typical big industrial company.

These are the same traits you find in most well-managed companies, whether they're in glamorous or prosaic businesses. Parker Hannifin Corp. is one of the most successful of the latter, having grown into a \$2.3 billion producer of hydraulic, pneumatic, and electromechanical parts. Its success has been based on a simple organizational principle: "When a division gets to a point where its general manager can't know and understand the business and be close to the customer, we split it off," says Chief Executive Paul G. Schlemer. Typically, that means plants of 300 to 400 workers, but there is no hard-and-fast rule on size. It has more to do with how well managers can deal with the organization's complexity. Parker Hannifin now has more than 200 plants in some 80 divisions.

SMALL PLANTS. It is a lesson many companies now entering adolescence have learned well. Worthington Industries Inc., consistently one of the steel industry's most profitable companies, expects to break the \$1 billion sales mark this year. But its management adheres to the idea that a single plant should never have

WHY A BIG STEELMAKER IS MIMICKING THE MINIMILLS



	Revenues	Employees	Three-year avg. annual ROE	Three-year avg. sales growth
LTV	\$7.6 billion	48,200	-11.6%	-1.2%
BIRMINGHAM STEEL	\$344 million	1,830	18.3	55.8

DATA: S&P PC COMPUSTAT PLUS

At the time, it seemed perfectly logical to LTV Corp. Chairman Raymond A. Hay. The union of his company with troubled Republic Steel Corp. in 1984 would sharply boost market share while creating dramatic cost efficiencies in production.

Meanwhile, James A. Todd Jr. had an entirely different notion—one that initially provoked snickers from such big producers as LTV. As head of Alabama-based Birmingham Steel Corp., Todd began buying up small inefficient steel plants in 1985. His goal: to build a

more productive "minimill" company that would convert scrap into finished steel products for niche markets.

There's little surprise in knowing who had the last laugh. Size only worsened the troubles already plaguing LTV and Republic. As Hay struggled to combine the two companies' differing cultures and bloated operations, the fast-plunging market sent LTV into Chapter 11 bankruptcy in 1986. Birmingham, by contrast, is thriving. Todd is expected to report some \$40 million in net income on more than

\$400 million in sales for the year ending June 30.

Behind Birmingham's success are typical small-company attributes: a genuine entrepreneur-boss, flexible work rules, cost-efficient facilities, and narrow product lines. Such advantages allow Birmingham to make a ton of steel with only a third of the labor man-hours of large producers.

Instead of the traditional eight-hour work shift, Birmingham's workers put in 12-hour turns, working three days one week and four days the next. That sharply boosts productivity by cutting time-consuming shift changes to two from three.

LOUDER VOICE. The benefits of smallness haven't been lost on Hay. He has drastically downsized LTV, trying to make it a leaner, more market-driven company. He even has adopted many minimill labor practices by giving employees such incentives as profit-sharing, stock ownership, and a greater voice in management.

Still, small rivals are expected to win more market share from LTV and the other industry giants. Experts predict that Birmingham and other minis will capture 36% of the market by 2000, up from more than 20% today. Vows Todd: "We are going to get a bigger piece of the market."



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more than 250 workers in it. The logic: The man on the floor should be able to go to the top to fix a problem before it gets too big. Not one of Worthington's 27 plants exceeds that 250 limit.

To retain agility and limit complexity, many executives have tossed aside the notion that self-sufficiency is a good idea. Vertical integration has given way to subcontracting. Why should an Apple Computer Inc. make memory chips or disk drives if outside companies can do it better? Apple Chairman John Sculley foresees a new corporate model built upon

interdependencies with other companies, suppliers, and spinoffs to gain greater flexibility. For every dollar of revenue that Apple generates, the outside network of companies that depend on Apple produce at least \$3 to \$4 in additional sales. But there can be a downside to this strategy. Apple's reliance on an outside supplier for memory chips led to a decision to stockpile them when a worldwide shortage developed. The company, however, paid near-record prices for the chips just as the shortage was easing, a miscalculation expected to knock about \$27 million

off pretax profits in the March quarter.

How are Japan's huge corporate entities run? Not as many assume. Like the best-managed big U.S. concerns, the better-run Japanese corporations are large collections of hundreds of individual companies. Matsushita Electric Industrial Co. boasts 161 consolidated units. Hitachi Ltd. comprises 660 companies—27 of which are publicly traded. "This is a very conscious policy," says James C. Abegglen, well-known authority on Japanese management. "As something new comes along, such as software, it gets moved out to a subsidiary so the elephant doesn't roll over and smother it. If all goes well, it becomes a successful company on its own. If not, it gets pulled back in."

BEHEMOTHS. To be sure, many industries remain in which economies of scale still apply. "A full-service global firm requires a strong capital base, superb operational capabilities, and great distribution to serve clients around the world," believes William A. Schreyer, chairman of Merrill Lynch & Co. "Because financial markets are global, a strong presence in the key financial centers of the world is critical to success." American Airlines, Boeing, Citibank, IBM, and Merck all are behemoths that combine size, efficiency, and natural economies of scale. Each is a world leader as a result of its global reach and power. In most cases, their existence does not preclude an aggressive upstart from capturing a niche.

Big or small, then, is hardly the issue. It's far more troublesome than that. As Alfred Sloan noted many years ago, size "is only a problem of management."

Is there an optimal size? Some pundits think there is. Michigan State's Adams says a telltale sign is when a company's profit margins dip below its industry's average. "Your company is too big when your people spend more time infighting over turf than paying attention to the overall mission," says Peter G. Keen, chairman of the International Center for Information Technologies. "An organization is too large when a CEO can't be personally heard. If you track the life of a piece of paper—whether a purchase order or a customer letter—the company is too big if it has to go through more than one intermediate step."

You can add myriad guidelines to any organization to decide if it is too big. But it still comes down to how well executives and managers run their business. Once asked how long a man's legs should be, Abraham Lincoln replied: "Long enough to reach the ground." No company's scale and scope should exceed the ability of its executives to manage the complexities of the business.

By John A. Byrne in New York, with bureau reports

THE BROKER WHO WOULDN'T GROW UP



	Revenues	Employees	Three-year avg. annual ROE	Three-year avg. sales growth
MERRILL LYNCH & CO.	\$11.0 billion	43,400	10.6%	23.1%
A.G. EDWARDS INC.	\$505 million	6,430	16.4	17.7

DATA: S&P PC COMPUSTAT PLUS

All the talk about global competition in financial services doesn't faze Benjamin F. Edwards III. The chairman of St. Louis' A.G. Edwards Inc. is committed to keeping his business close to its roots as a smallish regional brokerage. "Maybe it's out of ignorance," he says, "but instead of following the dollar, we've decided that we're in the retail brokerage business with a strong branch system—and that's what we're going to do."

Edwards eschews internal development of financial products for clients, steers clear of big-time dealmaking, and isn't willing to pursue a vast global network of offices—things that William A. Schreyer is likely to boast about as chairman of much larger Merrill Lynch & Co. "Our size has given us staying power and stability through a market breakdown," says Schreyer, alluding to the crash of 1987.

What it hasn't guaranteed Merrill is great profitability. Nearly 22 times Edwards' size, Merrill Lynch is an international powerhouse. Yet Edwards' net profit margins last year were

almost four times those of Merrill.

What's Edwards' secret? He chalks it up to focus. When the brokerage giants rushed off into real estate in the 1970s and early 1980s, Edwards stayed put. That business has since turned south for some brokerages. Merrill, unable in 1986 to sell its real estate operations outright, sold off a minority interest. "We didn't get the pleasure," says Edwards, "but now we don't feel the pain." Schreyer himself acknowledges that Edwards' success can be traced to its "stick-to-their-knitting" approach.

There's a simple lesson in all of this that small companies know full well: When you focus on only a few things, you can often do them better than someone who tries to do everything. Edwards spends more time figuring out how to provide better services to existing customers than looking for new areas of financial services to enter. Says Edwards: "It's like Vince Lombardi said—the secret is, they blocked a little better and they tackled a little harder. Results come from doing what you do better."

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EVEN HEROIC MEASURES MAY NOT SAVE MAXICARE

If the chairman's recapitalization plan doesn't fly, the HMO could face liquidation or Chapter 11

Since he was named chairman of Maxicare Health Plans Inc. last August, Peter J. Ratican has raced to resuscitate the health maintenance organization. His efforts have been heroic: Ratican has brought in a new management team, sold off health plans, and raised Maxicare's premiums.

But the patient has scarcely responded. Maxicare has lost about \$517 million in two years—\$260 million in 1988 alone. Long-term debt still tops \$286 million, and the company missed a \$36.3 million loan payment to Bankers Trust Co. in January. The lender has given Maxicare until Apr. 30 to devise a new payment schedule. Ratican has promised to unveil a recapitalization plan by the end of March. If he can't pull that off, Ratican says that he may have to liquidate Maxicare or even seek protection under bankruptcy laws. "If refinancing doesn't work, what choice do we have?" he asks.

BITTER PILLS. Ratican won't discuss the details of his recap. Options include persuading the company's bondholders and bankers to trade in some of their debt for equity. That's better than nothing, which is what debtholders would probably get if the company declares bankruptcy. But the plan is unlikely to please shareholders. Issuing equity would dilute their stock. Maxicare shares trade



RATICAN: LENDERS SET A DEADLINE

for less than \$1, down from \$28 in 1986.

Ratican's rescue operation developed further complications on Mar. 8, when he replaced Maxicare's investment banker, Goldman, Sachs & Co., with Oppenheimer & Co. That's Maxicare's third financial adviser in seven months. Neither Maxicare nor Goldman is talking, but insiders say Maxicare's board resisted the bankers' remedies. "They find it hard to take the medicine that Wall Street wants to give them," says one investment banker.

How did Maxicare end up on the critical list? Ratican inherited the mess from

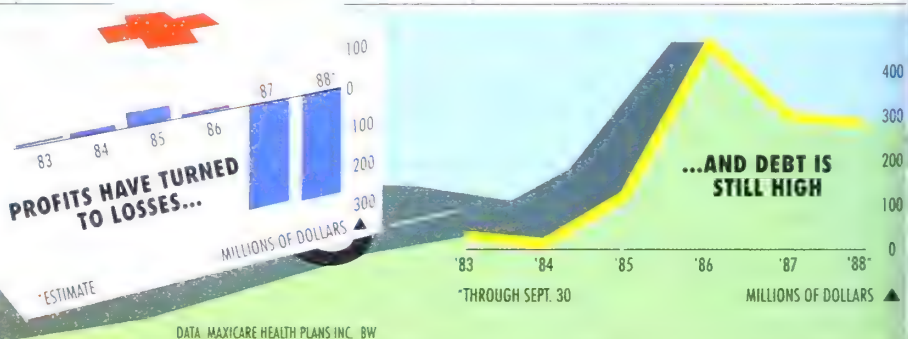
company founders Fred W. Wasserman and Pamela K. Anderson. The husband-and-wife team had parlayed \$37,000 investment into the nation's largest for-profit HMO. The company sold prepaid health care plans, mostly to employers who offered them as employee benefits. Wasserman hoped to build Maxicare into a national network by buying HMOs across the country.

BUYING SPREE. But the dream fell apart in 1986, after Maxicare acquired HealthCare USA, Inc. and HealthAmerica Corp., for \$446 million. The HMOs doubled Maxicare's enrollment to 2.3 million members. In 1987 its revenues hit \$1.8 billion. But both companies were in worse shape than Wasserman realized. And the buying spree helped push

Maxicare's long-term debt to \$464 million, just as health care costs soared and competition intensified. Wasserman, still a consultant at Maxicare, declined to be interviewed.

Ratican was tapped for chairman after Wasserman and Anderson resigned on Aug. 8. Although he had been a Maxicare director since 1983, Ratican, 45, had little experience in health care management. In 1967 he joined Price Waterhouse-U.S. where Maxicare was one of his audit clients. Later he handled accounting and finance for two Hollywood studios. Just before moving to Maxicare

WHY MAXICARE IS ON THE CRITICAL LIST

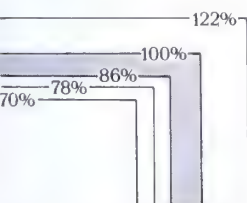




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but Confusion came instead.



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American Red Cross



Ratican served as chief financial officer at De Laurentiis Entertainment Group Inc. DEG filed for Chapter 11 protection soon after he left.

At Maxicare, Ratican's efforts seem aimed at avoiding the courts. He has dumped Wasserman's strategy of building a national HMO network, concentrating instead on California, the Midwest and the South. Maxicare has already sold 22 of its 32 plans for an estimated \$120 million. Proceeds from the sale have allowed Ratican to reduce Maxicare's debt. The auction has also helped him cut 2,200 jobs and squeeze administrative costs to 9% of revenues from about 12% last year.

UNPAID BILLS. That's not all. Ratican has hired McKinsey & Co. to improve a middle management team that made few decisions under Wasserman. To patch up relations with hospitals and doctors, Ratican is revamping the company's claims processing system to speed up its bill-paying cycle to 15 days from about 60. And he has increased Maxicare's premiums by an average of 32%.

But Maxicare may be caught in quicksand. Its rate hikes have averaged twice the increases of competitors, prompting some customers to flee. "It's like rat-jumping ship," says Dr. A. Hugh McLaughlin of Cuyahoga Falls, Ohio. The family practitioner lost 530 Maxicare patients in a year. Ratican has tried to stem the defections by making personal visits to corporate clients, but it hasn't helped much. This year alone Maxicare's enrollment at Illinois Bell Telephone Co. has dropped 67%, to 250.

Now, Maxicare has been prevented from giving itself transfusions: State regulators in California and Illinois have refused to allow Maxicare to funnel cash from robust plans in their states to needier subsidiaries. And some hospitals and doctors have already lost patience. On Mar. 1, University Hospitals of Cleveland filed a \$1.6 million suit against Maxicare's Ohio plan for failing to pay bills. "We've been misled too long," says University Hospitals' Senior Vice-President Gerald J. Haggerty. Maxicare says it is trying to negotiate a solution.

Ratican hasn't ruled out a worst-case scenario—he will consider liquidating the company if his recap plan fails. But he claims Maxicare's losses have begun to slow. If he can hang on to enrollees, he says, Maxicare could break even in 1989. The final word, however, belongs to Maxicare's debtholders, who will pass judgment on Ratican's refinancing idea. "I think we've got a shot," Ratican insists. By most accounts, however, Maxicare's prognosis is grim.

By Patrick E. Cole in Los Angeles, with Jon Friedman in New York



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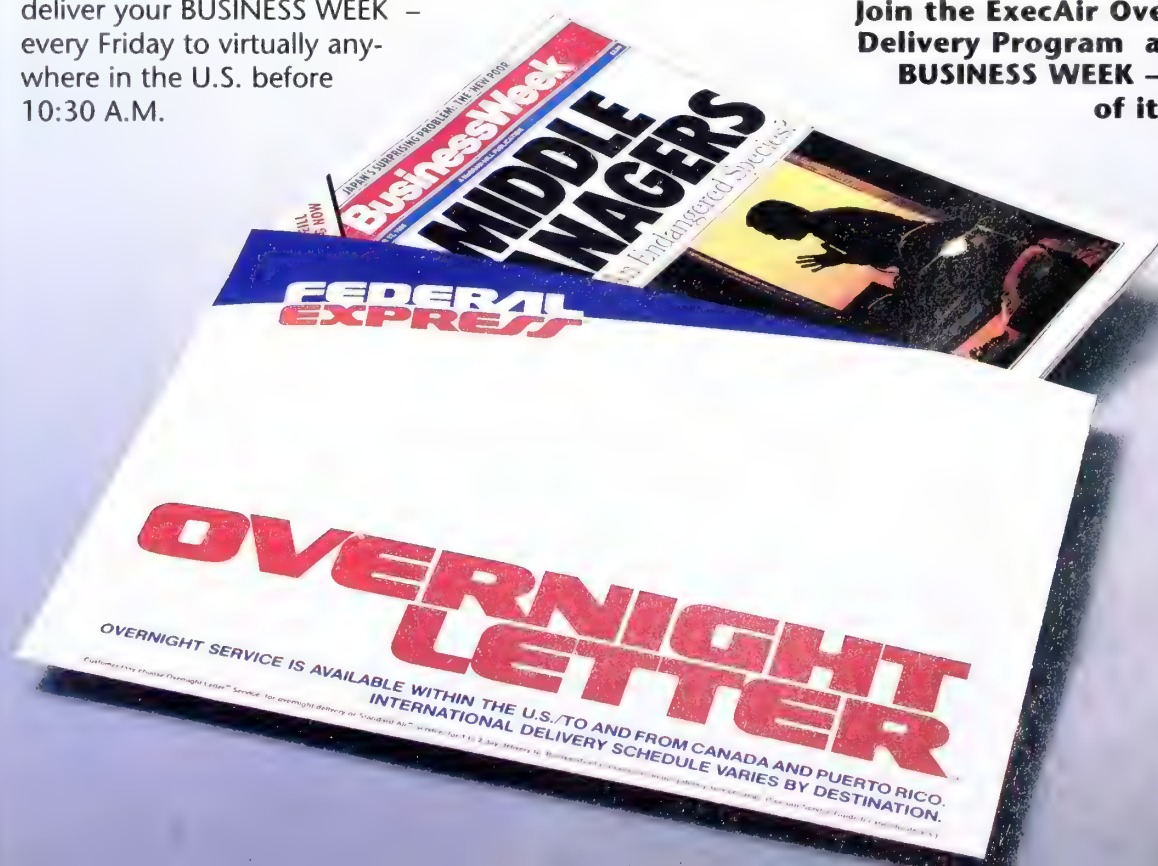
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THIS HOUSE PARTY IS WINDING DOWN

High interest rates and soft demand are putting a damper on prices

Go, get yourself a piece of ground, and hold possession.... You need do nothing more. You may sit down and smoke your pipe... and without doing one stroke of work, without adding one iota to the wealth of the community, in 10 years you will be rich.

—Henry George

More than 100 years ago, economist Henry George foreshadowed the real estate market of a generation made wealthy by soaring real estate prices. Home sweet home has not only been a great place to live but a superb investment as well. The nation's median home price jumped fourfold, from \$21,800 in 1969 to \$89,100 in 1988, while consumer prices generally tripled. There has been no place like home, at least as an investment.

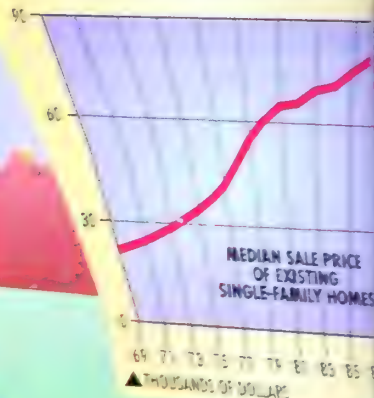
Housing mania is peaking, though, despite inflation's recent resurgence. The rate of price hikes for single-family homes has declined significantly during the 1980s (chart). Short-term, rising interest rates could put further pressure on the market as homeowners struggle to meet their interest payments on the more than \$500 billion in adjustable-rate mortgages (ARMs) outstanding. Ditto for debtors owing nearly \$100 billion on

home equity loans. In the longer term, demographic and economic forces will keep a lid on real estate appreciation.

Higher interest rates are already worrying home buyers who took out adjustable-rate loans during the past few years. "They'll face real payment shock," warns Warren Lasko, executive vice-president of the Mortgage Bankers Association of America. Eric Greenstein, president of a small executive-search company outside Boston, took out a big \$300,000 ARM in 1985. He expects that his mortgage rate will ratchet up by two points come August, boosting his yearly mortgage payment by some \$6,000. "The rate increase is going to strangle me," says Greenstein.

LESS DEMAND. Over the long haul, demographic trends, too, will dampen housing price gains. The 76 million baby boomers born between 1946 and 1964 helped fuel the home-buying binge that began in the 1970s. Home lust among baby boomers will be partly satiated in the 1990s. The baby-bust generation, the 41 million born between 1965 and 1976, will exert less pressure. And mind-boggling home price gains in metropolitan areas could slow local economic growth and contain real

HOUSES KEEP GETTING COSTLIER...



estate values. The first-time home buyer, for one, is priced out of a good number of economically important cities and their environs.

That is the bad news for homeowners. Now for the good news: Home prices aren't about to fall off a precipice. National home sale prices will at least track inflation. A BUSINESS WEEK survey of real estate markets around the country shows that most are in decent shape with modest price increases and reasonably brisk sales. Indeed, there are signs that prices in the major regional markets will move closer together over time as previously troubled markets recover and the hot markets peak.

The exception is California. It's in the throes of a fever-pitch boom. Prices of homes shot up by 32% in Los Angeles last year, lifting the median sales price to \$180,100. The San Francisco region saw prices rise by 28.1%, to \$206,500. Stoking California's hot market are job hunters and a growing crop of laws restricting development.

SIGNS OF LIFE. Many of the nation's worst markets are starting to show some signs of improvement. Median sale prices overall fell by 5.3% last year in Denver. But "there has been a tremendous improvement in sales of existing homes in the past 10 months," says Tucker Hart Adams, chief economist for Central Banks of Colorado. Just ask Joe Louis Barrow Jr., consultant and author of a

DENVER: ARE THE DOLDRUMS OVER?

One of the nation's most depressed real estate markets seems to be recovering slightly. It took Joe Louis Barrow Jr., son of boxer Joe Louis, just one month this year to find a buyer willing to spend \$280,000 for his remodeled carriage house



...BUT THE BREATHTAKING GAINS ARE GONE



DATA: NATIONAL ASSOCIATION OF REALTORS

FOR
SALE

ography of his father, famed boxer Joe Louis. On Jan. 25, he put his remodeled marriage house in Denver on the market for \$289,000. A scant month later he sold for \$280,000.

In the Northeast, however, the boom never over. Boston home prices went from year-to-year gains of 35% in the mid-80s to an anemic 2.4% last year. Prices will stay flat to slightly lower in New England, says Gary L. Ciminero, chief economist at Fleet/Norstar Financial Group Inc. In the New York City area, with a loss of roughly 20,000 jobs in the financial-services sector after the 87 market crash, prices squeezed out a 1% gain for the year, but fell by 3.6% from the fourth quarter of 1987 to the same period in 1988. The Northeast's cluster market even helped cool off Florida. "When it's soft up there, drop in demand is sure to be felt here," says real estate economist Lewis M. Goodkin.

Indeed, some worry that the Northeast's worsening market is a harbinger of a nationwide real estate crash. For instance, Comstock Partners Inc., a New York-based money management firm, believes that real estate could fast become a depreciating asset. After all, says Comstock partner Michael Weinstein, "you can't say it's just a regional problem" since the Northeast accounts for some one-quarter of the nation's housing market.

Yet home-price weakness in the Northeast isn't about to snowball into an avalanche of collapsing

prices that could bury the nation's economy. Instead, the workings of supply and demand suggest a stagnant market for several years.

First of all, real estate prices typically don't plunge absent a calamity, such as the Great Depression. More recently, plummeting oil prices sent the Southwest into an economic tailspin just as a home-building boom was going full tilt. By contrast, the Northeast "is a strong diversified economy that's not about to fall apart," says Wellesley College professor Karl E. Case. And many home sellers will take their "product" off the market if they don't like the price.

Helping to hold up prices are a panoply of local rules and regulations limiting the supply of new housing. Many folks in New York and Boston, for example, resist multifamily housing projects in their suburban communities as fiercely as they would a penitentiary.

BIG DISPARITY. Keeping a tight rein on price increases is the glaring disparity between prices and incomes. The time-honored rule is that a household can afford to pay about 2.5 times its annual income to buy a house. According to a Salomon Brothers Inc. report by Anthony Downs, senior fellow at the Brookings Institution, the median price in the New York area in the third quarter of 1988 was an astounding 7.1 times median income. It was 4.5 times income in Boston, 4.4 times in Providence, and 4 times in Hartford. "High housing prices are affecting the growth rate of certain economic areas," says Downs.

Astronomical housing costs make it difficult for employees to move into the Northeast. Take the experience of John and Barbara Jago-Ford. John, a national sales manager for Rostra Tool Co., moved from Florida to Connecticut last fall. They took a net \$8,000 loss on sell-

ing their four-bedroom colonial for around \$100,000 in the weak Orlando market in February. After months of searching for a comparable house they could afford, they finally found a builder willing to erect one in Madison for \$264,000—after he cut the price by \$30,000 to get the work. Even then, the Jago-Fords barely qualified for an 8% ARM that adjusts upward in six months.

Many employees living in other regions are refusing to relocate. Some companies have decided that if their employees won't come to them, they'll move. J. C. Penney Co., for one, left New York City for the Dallas area.

It's not just a Northeastern problem. "Moving employees into California is very tricky," says Leonard Troutner, an executive at Coldwell Banker Relocation Management Services Inc. in Laguna Hills, Calif. In the so-called Research Triangle of North Carolina, the mayors of Raleigh and Durham recently joined representatives from banking, real estate, and nearby universities to form the Triangle Housing Partnership. Its mandate: help create affordable housing for moderate-income folks. The *Harvard Business Review* recently focused on the "convulsion in U.S. housing" that's adversely affecting businesses.

America's wealth is largely tied to the home. Some 64% of households own their own home—with a median sales price of \$89,100. That compares with the meager 10% that own stock portfolios exceeding \$5,000 in value. Americans need not worry that the value of their biggest asset is going to collapse. The worry now is making sure the American Dream doesn't become just a dream to the young and less-than-wealthy home-seekers in strong local economies.

By Christopher Farrell in New York, with bureau reports



STICKER SHOCK IN CONNECTICUT

■ Relocating to the Northeast was a jolt for John and Barbara Jago-Ford. They took a net loss on the sale of their Orlando home, spent months house-hunting, and ended paying nearly three times what their old house brought in

THE 'TOXIC WASTE' OF THE THRIFT CRISIS

Ailing S&Ls have \$300 billion in problem properties

It was the toughest real estate project that turnaround specialist Walter R. Barnes had ever taken on. Most residents of San Diego's Harbor Vista, a 272-unit low-income housing complex, had defaulted on their mortgages, and the place had become a supermarket for drug dealers. Barnes and his team went in with shotguns and police dogs and started evicting squatters, scrubbing off graffiti, and renovating burned-out units. It took two years. Only then were the lenders who had hired Barnes able to avoid a total write-off, instead selling the repossessed units at a loss of only 30¢ on the dollar.

Imagine thousands of Harbor Vistas across the nation, and the savings and loan crisis becomes more than a matter of Washington haggling over the price tag. The thrift crisis is also a matter of scraping paint and staving off vandals, of finding reliable tenants or viable buyers—all on an immense scale.

'D-DAY.' As much as \$300 billion of sour real estate is on the books of insolvent or teetering thrifts. So whether the Administration's rescue package costs taxpayers \$90 billion, \$150 billion, or far more hinges to a large extent on how much the government can recoup from selling these properties. So far the regulators have scarcely addressed the maintenance and marketing of this real estate. "This is unlike any problem they've seen before," declares John A. Koskinen, president of Palmieri Co.

The Federal Savings & Loan Insurance Corp. seemed to take a half-step toward getting outside help when Congress created the Federal Asset Disposition Assn. in 1985. But FADA has been hobbled by bureaucratic infighting (its private-sector recruits were better paid than FSLIC regulars), controversial lead-

ership, and overhead that proved too high. It took on \$4 billion in property but has only sold \$1.5 billion worth.

Fortunately, there is a network of real estate "workout" companies anxious to fill the vacuum. If they handle the troubled properties deftly enough, they can turn a profit—and save taxpayers a bundle. But the task is daunting. Cataloging and selling the stockpile of properties will require colossal computer systems.

try," says Crocker. "They don't want you to know they produce it, much less where they dump it."

Under pressure from the industry FSLIC has played the same game of warehousing instead of selling its real estate. It now manages \$3.5 billion worth of property, has farmed out \$7.9 billion to private workout companies and still oversees some \$60 billion in property held by thrifts that were sold in federally assisted mergers.

HOLDING THE BAG. Unfortunately, warehousing more property only lets the problem snowball. And the costs of misjudging the market can be enormous. In 1984, FSLIC took over a \$10 million loan for a major hotel in a Midwestern town. FSLIC had the chance to sell the note back to the original borrower for \$8 million. The agency declined because it wouldn't have been getting full value. But no buyer has come along since



Battalions of lawyers must untangle legal titles and skirmish in litigation and bankruptcy proceedings, and skilled managers must oversee restoration and security. "Mobilizing the resources to fight this problem takes the same kind of effort as preparing for D-Day," declares Donald W. Crocker, president of J. E. Robert Cos., an Alexandria (Va.) real estate concern.

The S&L industry has been papering over problem real estate for years. Facing up to loan losses would have ruined balance sheets, while seizing and selling off the properties backing the loans would have battered property values and crushed healthy and sick thrifts alike. "This is the toxic waste of the S&L indus-

and FSLIC is still in the hotel business

To succeed, federal agencies and private operators alike may need to invest heavily—and patiently. Consider Indigo Run, a 2,000-acre resort in Hilton Head S. C. Its developer entered Chapter 11 in 1986. That toppled Southern Florida Bank in Boca Raton, which had lent the developer \$65 million for a leveraged buyout and sunk \$45 million in outlying parcels of the half-finished resort.

Washington (D. C.)-based Oaktree Capital Inc., which FSLIC hired to manage Southern Florida Bank, persuaded the agency to buy Indigo Run for \$12.3 million. That opened the way to full development, which could salvage the thrift's investment. Now, three years

er, the completed project boasts 5,500 identical units and room for 2½ golf courses. Oaktree hopes FSLIC will get \$10 million for the property.

A smaller operator, Skyline Financial Services Corp., of Falls Church, Va., has hoped to revive Houston's Glen Iris subdivision, not long ago a suburban ghost town where vandals stole every air conditioner and fence in sight. The firm closed out foreclosed homes and, after the community stabilized, started selling them to tenants. Houses originally valued at \$50,000 now go for about \$22,000, a 56% drop from the \$18,000 they would have fetched 18 months ago when Skyline stepped in. "The best thing to do is to maintain the raw value in the home by keeping a tenant in there," says Skyline Chairman Stuart A. McFarland. "To leave homes boarded up is like a cancer that will spread out of that subdivision." Chairman L. William Seidman of the Federal Deposit Insurance Corp., who takes overall charge of the thrift crisis under the Bush rescue plan, insists that he'll take a different approach. Instead of keeping real estate under government supervision, he wants to sell properties quickly. "Our basic policy is that every asset we have is for sale at current appraised value," says Seid-

Battalions of lawyers must untangle legal titles. Then the real work begins—salvaging neglected houses

1. "We don't believe we are in the business of speculating on asset value," says Seidman. But he will have trouble liquidating large amounts of real estate quickly. Getting buyers to pay the appraised value in depressed markets is not impossible. And there are always unpredictable events that delay even the best real estate operators.

When New York-based Eastdil Realty stepped in to turn around a vacation-home development on the Northern California coast, it got a nasty shock. The project had been built on the habitat of the long-toed salamander, an endangered species. Eastdil hired Stephen B. Hahn, a salamander expert at Monterey Peninsula College, to help find ways to protect the black-and-orange-spotted amphibian. After a one-year study, the development was redesigned to include retreat areas for salamander mating. But the problem isn't the government, the biggest problem isn't salamanders. It's a vast lot of white elephants. And they'll take a lot of care and feeding.

By Catherine Yang in Washington



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What movie will be the blockbuster of 2007 A.D.? Hard to say. But one thing's for certain. Samsung VCRs will definitely be getting rave reviews.

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THE BUSINESS THAT BROKERS WOULD LOVE TO DITCH

Morgan Stanley says many trades for institutions don't pay

Wall Street trembled in the mid-1970s when Washington ordered an end to fixed commissions on stocks. Many small firms folded, but the survivors found that the discounted rates spurred an explosion in trading, especially by big institutional investors. Eager to get larger shares of the burgeoning market of the 1980s, brokers kept on lowering their commission rates (chart). Well before the 1987 crash,

firm has followed suit publicly; officials at Merrill Lynch, Shearson Lehman Hutton, and Prudential-Bache all disavow any retrenchment in stock trading. "We have not cut back," says Stanley B. Shopkorn, head of equities at Salomon Brothers Inc. "But we continue to review the economics of what has become a very difficult business."

The conventional wisdom holds that big brokers have to trade for institutions

president of Integrated Resources Asset Management. Positioning is a practice by which, to speed up a trade, a broker uses his own capital to buy all or part of a client's shares. Positioning provides important liquidity to the stock market. Brokers say they lose money in positioning, but they do it in the hope that clients will reward them with the easy, profitable, "no-brainer" trades.

Big brokers are now less willing to position stocks and provide liquidity because money managers, under pressure from clients to cut commission costs, are reluctant to pay a decent price on routine trades. Instead, they are shunting more of the no-brainers to such bare-bones institutional discount brokers as Abel/Noser Corp., which executes the orders for 2¢ to 4¢ a share. Institutions are also trading through "soft-dollar" brokers like Autranet Inc. and Lynch, Jones & Ryan. Soft-dollar brokers will, for a

specified number of commission dollars, set up money managers with stock-quote terminals or data-base services and provide pension-plan sponsors with custodial or consulting services.

LOWER QUALITY. Some money managers worry that the trend toward ever lower commission rates can result in clumsy executions. Suppose an institution chooses a broker to save a nickel a share in commissions. What is saved if the cheaper, but less skilled, broker executes the trade at an eighth-12½¢ a share—higher than the more expensive broker will do? And Dave H. Williams, chairman of the giant Alliance Capital Management Corp., observes that lower commissions have hurt the quality

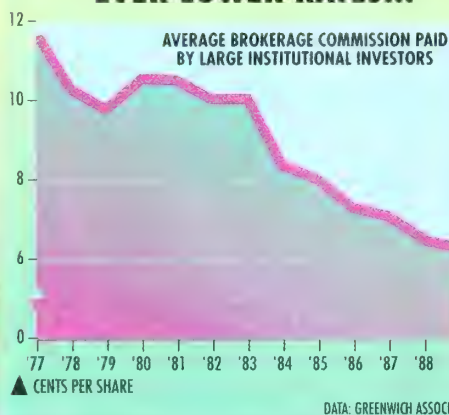
of investment research. Written reports, visits from analysts, and telephone updates are part of the service that the big brokers now provide.

The pressure on commissions will continue to reshape Wall Street. Big brokers may have to "unbundle" their services by cutting rates further but charging clients explicitly for investment research, a move they have been loath to take for fear customers won't pay for what they now get for free.

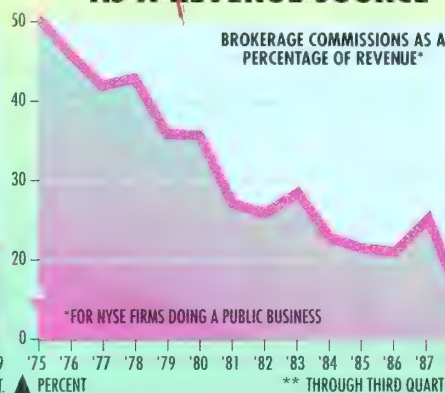
The brokers may also abandon commissions altogether and instead trade Big Board stocks the way they now trade bonds and over-the-counter issues—making their profit by marking up their inventories. New York Stock Exchange rules prohibit members from doing that now. But history shows that if economic forces demand it, the Big Board will find a way to permit it.

By Jeffrey M. Laderman, with Jon Friedman, in New York

AS INSTITUTIONS PAY EVER LOWER RATES...



...COMMISSIONS SHRINK AS A REVENUE SOURCE



DATA: GREENWICH ASSOCIATES, SECURITIES INDUSTRY ASSN., BW

say some Wall Streeters, the core business of trading the likes of IBM, GM, AT&T, and other Big Board stocks was a breakeven proposition at best, and a loss leader most of the time.

Now some brokerages are beginning to question whether they need—or can afford—that loss leader anymore. Morgan Stanley & Co. is turning heads on the Street with a report grandly entitled *The Coming New Era in the U.S. Equity Business*. The message: Morgan Stanley will now lavish such services as research and block trading only on its most profitable institutional clients. The lesser ones are, in effect, being told to take a walk. If they stay with Morgan, they will be relegated to the Individual Investor Services division, where they won't receive the same treatment.

"Morgan Stanley's thoughts are on everybody else's mind," says Jay Bennett, a principal at Greenwich Associates, a consulting firm. No other big

to assure that they will be customers for the firms' initial public offerings. But with underwriting in a slump, some firms are questioning the cost of maintaining large sales networks. Instead, they prefer to invest in higher-margin activities such as junk bonds, bridge loans, and leveraged buyouts.

POSITIONING. Some retrenchment is inevitable. Industrywide, commissions now make up less than one-fifth of revenues. And it's not going to get better anytime soon. Total commission dollars spent by the 750 largest institutional investors dropped to about \$2.5 billion in 1988, down 26% from 1987, according to Greenwich Associates. The institutions project only a 3% increase this year, and they expect to trade at an average 6.3¢ per share, down from 6.5¢ in 1988.

Cheap commissions are not an unmixed blessing for the institutions. "You can't find anyone to 'position' stocks for you anymore," complains Harvey Eisen,

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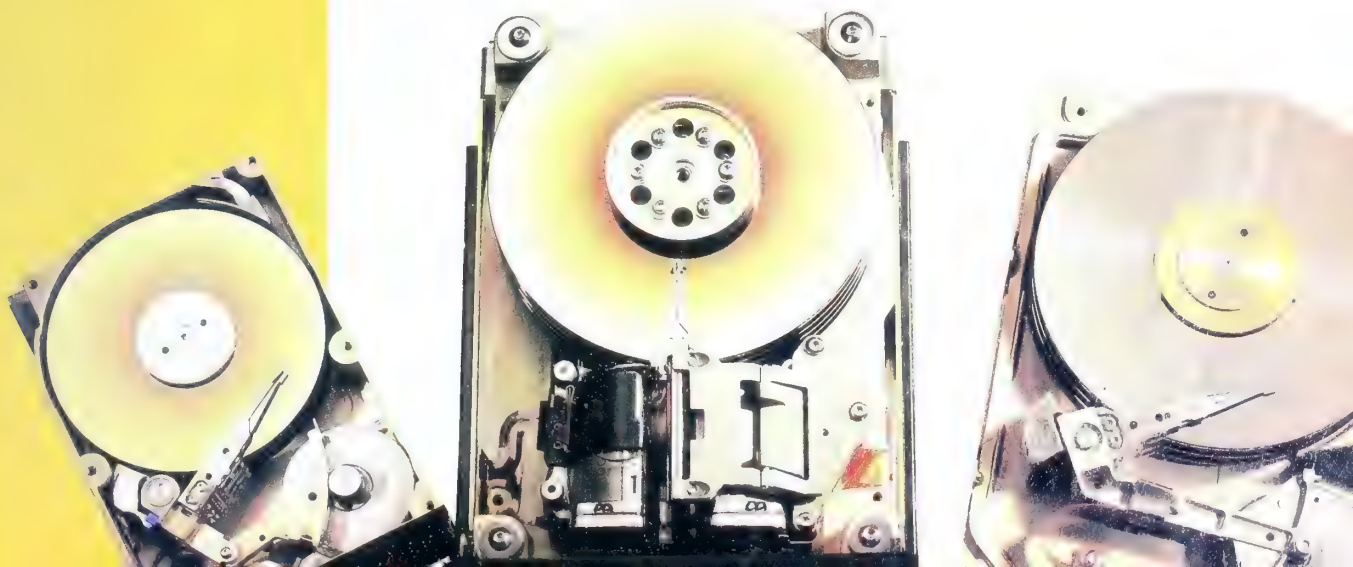
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BY GENE G. MARCIAL

THE STREET'S VIEW OF COLGATE NEEDS BRUSHING UP

Despite its visibility as a worldwide producer of popular household and consumer products, Colgate-Palmolive hasn't been a hot property on Wall Street. The stock's all-time high was only 52—and that was back in 1987, just before the October crash. The shares have been in a rut so far this year, trading between 43 and 47 since November.

That suits some savvy investment pros—and recent buyers—just fine, though. Says one New York money manager: "Any way you slice it, the stock is grossly undervalued based on the values of similar companies that have been taken over."

Joe Kozloff, an analyst at Drexel Burnham Lambert, agrees. The maker of such well-known products as Colgate and Ultra Brite toothpastes, Fab laundry detergent, Ajax cleanser, and Palmolive soap "has a pretty unique franchise and a highly regarded management," says Kozloff. He puts the private-market, or breakup, value of Colgate at around \$75 a share.

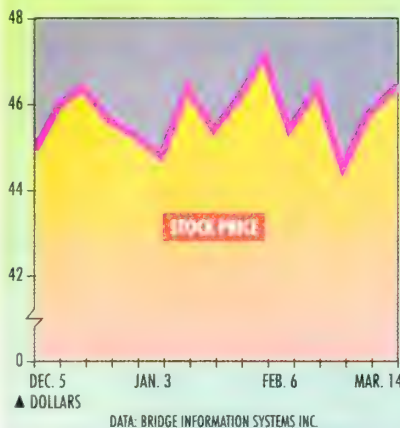
Kozloff estimates that Colgate's profitable and rapidly growing Hill's Pet Food division is worth some \$1 billion on its own. Beyond that, the company's assets are not easy to quantify, Kozloff admits. Clearly, though, Colgate's brand franchises, particularly in toothpaste, plus its domestic and international distribution network "are quite valuable."

In fact, some 60% of sales come from overseas. Also hard to quantify are Colgate's extensive real estate properties both at home and abroad. Takeover experts estimate that if Colgate were valued at the industry's historical takeover multiples, it would be worth \$70 to \$80 a share.

CLOSER TO HOME. The "key to Colgate's new allure is the swing in its profit margins," says Stuart Shikar, managing director of Prudential-Bache Investment Management, who has been buying the stock. He notes that Colgate is paying more attention to improving the bottom line.

After the sale of the Kendall Health Care division in 1987 for nearly \$1 billion, management started refocusing on Colgate's basic businesses to bolster domestic operations. Shikar estimates

COLGATE-PALMOLIVE: MOVING IN A NARROW BAND



that earnings will jump from last year's \$2.84 a share to \$4 this year, and to \$4.75 in 1990.

Colgate shares come "under heavy accumulation by the big players" whenever it drops to the low 40s, notes one trader. Although Shikar says he isn't aware of any new takeover interest, he concedes that if Colgate announced that it would consider bids, about 25 suitors would quickly surface. Last year, Colgate was rumored to be a target of several raiders, including Revlon Chairman Ron Perelman.

More recently, a European chemical company was whispered to be interested in a stake in Colgate or in a takeover bid. Institutional investors own 51% of the stock, while management own a paltry 1% of the 68.5 million shares outstanding.

THIS MINING BUY IS ON SOLID GROUND

Metal bugs who latched on to shares of Falconbridge, a large Canadian mining company and the world's second-largest producer of nickel, certainly have made a bundle. The stock shot from 15 in September to 25, buoyed mainly by escalating metal prices. But Falconbridge, which also mines zinc, cobalt, and precious metals, isn't just a metals play, and that's why Andrew Brichant, an analyst at Ladenburg Thalmann, thinks the stock is still a bargain.

Falconbridge has loads of "free cash," which invariably attracts raiders. Brichant estimates cash from operations, which in 1988 totaled \$535 million, or \$7.15 a share, at \$585 million, or \$9 a share, for 1989.

With revenues expected to grow this year by 17%, to \$2 billion, Falconbridge is expected to continue buying back shares; the company repurchased 21.7 million shares in 1988. One reason: Noranda, another Canadian mining company, has acquired a 23% stake and has said it intends to buy an additional 10.8%. Management owns about 1%. "We assume that Noranda intends to take over Falconbridge at \$35 to \$40 a share," says one New York money manager. He thinks Noranda may do it as a defensive move, since it is deemed a takeover target by an Australian mining company.

Brichant feels that, based on business fundamentals, Falconbridge can rise to 30 in no time. He notes that the company has plenty of zinc, "which is today's hot metal. Its price has been on the fast track."

CLEAR SIGNS TO SELL SHORT

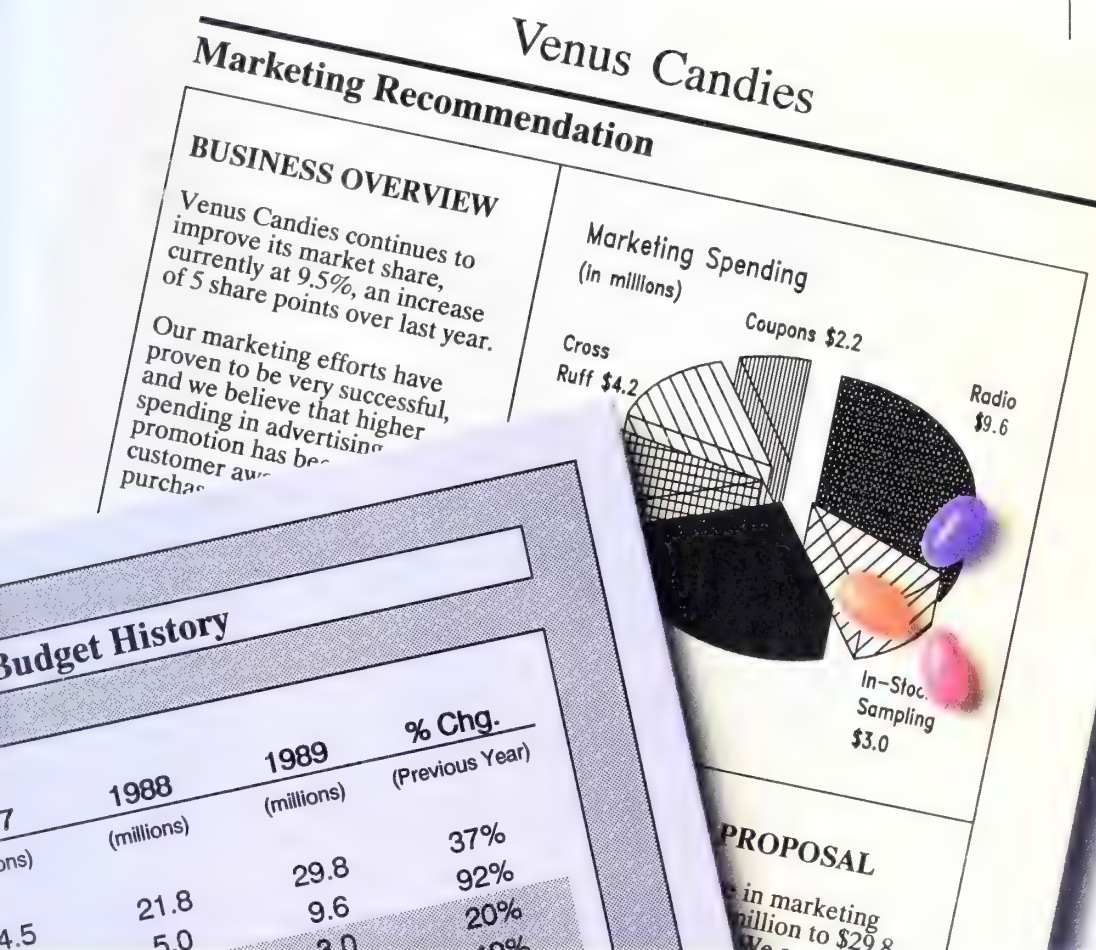
With shares of Casey's General Stores having fallen from 16 in mid-1988 to 11, you would think the shorts would be patting themselves on the back. But they say the stock has to drop to 8, if not lower. The earnings of this operator of more than 650 convenience stores and gasoline stations in eight Midwestern states fell below Street expectations for the fiscal third quarter that ended on Jan. 31. Chairman Donald Lambert argued that net was down despite a jump in sales because of competitive pressure—and reduced profit margins—on gasoline. He expects earnings to pick up in subsequent quarters.

But one New York investment adviser figures that the stock, which now sells for twice book value, is still overvalued. "The company's problems will be worsened by rising gasoline prices," he warns, "which will further pinch profit margins." He thinks Casey's faces "a tough fourth quarter."

Chris Vroom, an analyst at Alex. Brown & Sons, has cut his estimate for fiscal 1989 to 89¢ a share from \$1, vs. last year's net of 88¢. For 1990 he reduced his \$1.17 estimate to \$1.10. Apart from rising gasoline prices, Vroom thinks margins are being crimped by Casey's increased spending for its fast-food operations.

The bears note that Chairman Lambert sold 56,000 shares in December and another 56,000 in February. But he still owns 20% of the 11.4 million shares outstanding.

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THE UAW REBELS TEAMING UP AGAINST TEAMWORK

A big bloc of auto workers, fed up with union-management cooperation, is fighting back

At the huge General Motors Corp. engine and assembly complex in Pontiac, Mich., leaders of Local 653 of the United Auto Workers thought they had done everything right. Intent on saving jobs by driving down costs, they nurtured team production systems, relaxed work rules, and backed union-management cooperation.

But instead of the approval they expected from members, union executives were dealt a stunning defeat in the March election of delegates to the union's convention next June. Hard hit by layoffs, workers overwhelmingly voted for candidates who had lobbied against concessions and cooperation with the company. "We'll have to look at the things we're doing," says Richard W. Long, the local's vice-president. "If we don't see that, we're fools."

EMOTIONAL RALLIES. The discontent spreads far beyond Pontiac. Throughout the UAW, an increasingly vocal group of dissidents is challenging the move toward labor-management cooperation led by the union's leadership. It's the UAW's fiercest internal debate in 40 years. Their gripes are affecting management, too. Shock waves from the struggle could hamper auto industry efforts to boost productivity through increasing involvement by hourly workers.

Most vulnerable is GM, which has been pushing hard to cut its bloated costs with cooperation and team systems. "They're mistaken if they [GM] don't think they're going to get the backlash of this," says one UAW official who backs the union leadership. And if the dissidents gain ground at Ford Motor Co. and Chrysler Corp., "then the storm warnings really go up," says former UAW President Douglas A. Fraser.

Dissent, of course, is not new to the UAW. This time, though, there's a difference. The rebels are more united and sophisticated than in the past. Campaigning under the "New Directions" label, they have drawn hundreds of members to emotional rallies around the country. And they have gained the support of Victor Reuther, the brother of the late, legendary UAW president, Walter Reuther.



WHAT THE DISSIDENTS CHARGE

Concessions have not saved jobs. Two GM plants are "indefinitely idled," despite a contract provision against plant closings.

GM wins contract changes by pitting locals against one another to bid for a shrinking amount of work.

Work teams are a means of eliminating jobs, which forces union members to work harder.

Locals discourage worker grievances and fear loss of jobs if they appear "uncooperative."

Joint labor/management programs have created a bureaucracy of union appointees who are not directly accountable to the membership.

DATA BW

Reuther has accused UAW leaders of selling out to management by embracing cooperation without demanding enough in return. His alliance with the dissidents has provoked so much concern that five top former UAW leaders, including Fraser and Leonard Woodcock, another ex-president, late last month took the extraordinary step of sending UAW members a letter denouncing Reuther's attacks.

The big test of strength will come at the June convention, when members of the union's 22-person executive board are up for reelection. The dissidents first sought a seat on the board in 1986, when a local leader named Jerry Tucker narrowly lost an election. Tucker challenged the vote, but the union leadership ruled against him. He finally won his seat only last year after a long court battle. Tucker is running again in June, and once more the leadership is fielding a opponent.

NO 'WHIPSAWING.' The dissidents are backing at least one more candidate, and their strength has already rattled the incumbents. A strong new challenger is Don G. Douglas, president of Local 594 at a truck plant in Pontiac. Douglas swept delegate elections at two locals in early March, including the one at the Pontiac engine complex. The rank and file, says Douglas, "have been beat over the head with concessions. They're trying to send a message that it's time for a change."

For management, the real trouble will come if the UAW backs off from teamwork and cooperation. New Direction leaders say they may push for proposals at the convention that would make it harder for management to install teamwork or cut down on the number of job classifications. They want stronger provisions against "whipsawing." They say automakers pit plant against plant by threatening to close or scale back factories that won't change traditional work practices. In addition, the dissidents want to end multiple voting on contracts. They claim this often happens when union executives try to ram a contract down members' throats.

The opposition is gaining visibility just

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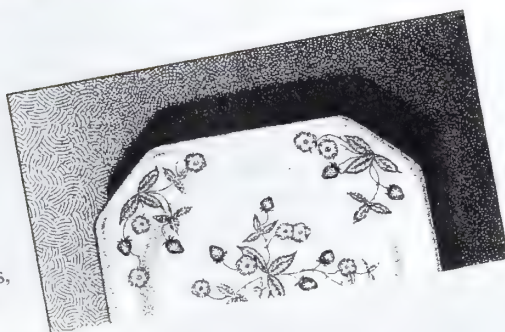
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This Panasonic 27-inch color TV, complete with "Early American" style wood cabinet, now finding a home in Japan.

How TV sets from the U.S.A. are now making it in Japan.

... began last June. A shipment of Panasonic 27-inch color TV sets—not imported from Japan—but exported to Japan. It was a bold signal that the Japanese market is ready to buy more goods from the U.S.A. A signal sent by Matsushita (pronounced Mot-SOOSH-), one of the world's largest electronics companies. But Matsushita is doing more than importing products from the U.S.A. It is also helping American companies that manufacture everything from computers to cosmetics to sell their products in Japan.

... the Governor of Illinois said, "At a time when we hear so much about the balance of trade between Japan and the United States, it is encouraging to see American workers producing a product for export to the Japanese consumer market."

Another speaker said it differently, "We're building them here and shipping them there."

FROM ILLINOIS TO JAPAN

... both were speaking about 5,000 TV sets from the U.S.A. headed for the Japanese home market. The 27-inch sets from Matsushita Industrial Company in Franklin Park, Illinois, are not only assembled in the U.S.A. but 70% of their components, including the picture tubes, are American-made products. Equally important, the product was designed in the U.S. specifically for

the Japanese market. To date, sales of the handsome wood cabinet sets in Japan have been encouraging.

Matsushita's involvement in strengthening U.S.-Japanese ties is part of a long company tradition that includes everything from establishing plants in Illinois, Georgia, Tennessee and other states, to funding professorships at MIT, Harvard and Stanford.

HOW AMAC CAN HELP SELL YOUR PRODUCT IN JAPAN

Indeed, Matsushita has formed a company—AMAC—whose major purpose is to help sell U.S. products in Japan. AMAC can help your company redesign a product to fit Japanese needs, arrange export licenses, set up introductions to key people, even help sell your product in Japan.

This recognition of international trade as a two-way street is part of a larger corporate philosophy—a philosophy that emphasizes "Human Electronics."

HUMAN ELECTRONICS

Matsushita Electric is devoting its research and development efforts to the concept of Human Electronics. Matsushita's objective is to develop and market products that make life richer, safer and more comfortable. In fact, we have developed over 14,000 products that are successfully fulfilling that goal. These products are sold worldwide under the brand names Panasonic, Technics, Quasar and National. In 1987, Matsushita's consolidated sales volume surpassed \$38.5 billion. All a direct result of a single-minded philosophy: Don't create new technology for technology's sake, but for man's sake.

MATSUSHITA ELECTRIC
PANASONIC TECHNICS QUASAR NATIONAL

when the "team" movement seems to be paying off. Before contract talks in 1987, GM officials hinted that they could be forced to cut more than 50,000 jobs at components plants if those factories didn't boost efficiency. Management argued that much of the work could be done more cheaply by outside or foreign contractors.

Now "the steep trend toward outsourcing has clearly been slowed," says Daniel D. Luria, an analyst at the Industrial Technology Institute in Ann Arbor, Mich. Union leaders credit union/management committees, which have found ways to boost productivity. But if the dissidents prevail and union members refuse to participate in such committees, GM could quickly face competitive problems again.

POWER VACUUM. The New Directions campaign may profit from GM's lackluster sales. The auto maker currently has the capacity to produce 45% of the U.S. car market. But it has captured only 35% of market share. Industry analysts say management may have to close permanently as many as four assembly plants. Indeed, although the current contract contains a ban on plant closings, two plants are on "indefinite idle" because they don't have enough work. More than 43,000 workers have already been laid off. Although teamwork has saved many jobs in components plants, the layoffs send a conflicting message to union members: that cooperation isn't paying off.

The controversy comes at a time when UAW's leaders seem ill-equipped to handle it. Owen Bieber, the union's president, is a cautious leader who has spoken out on both sides of the issue in recent years. This doesn't matter so much while Donald F. Ephlin, a UAW vice-president, is in charge of the union's GM department. He embraces cooperation and fights hard to get the word out to members.

Ephlin, however, has decided to retire in June, in part because he is tired of fighting without strong support from his union peers. His likely successor, Stephen P. Yokich, now vice-president of UAW's Ford department, has long kept his distance from teamwork and joint programs. As a result, there's a vacuum at the top just when the opposition is gaining ground. "We're hamstrung," says one union official. "It's a very painful time."

How GM and the UAW come through the storm will determine whether this is the last gasp of the traditionalists or the beginning of a new militance that could roil the industry. One lesson is already uncomfortably clear: The loyalty of many union members is still up for grabs.

By Wendy Zellner in Detroit

Information Processing

SOFTWARE

'THE UNIX WAR' IS OVER —BUT THE FIGHTING GOES ON

The competition has shifted to key software features

The first engagement in what became known as "The Unix Wars" occurred a year ago, when IBM and Digital Equipment formed an unprecedented alliance against AT&T. It had become apparent that American Telephone & Telegraph Co.'s Unix operating system, basic software that runs on everything from PCs to supercomputers, would become a fixture in the 1990s. The original IBM-DEC group, seven companies known as the Open Software Foundation, wanted an IBM version of Unix to be an alternative to AT&T's original. OSF argued that its Unix would be an open standard, meeting the needs of many computer makers—not just those of AT&T and its partner, Sun Microsystems Inc.

But suddenly, that battle is almost irrelevant. AT&T has formed its own consortium, called Unix International, eliminating concerns that

AT&T's club was a closed one. Unix International plans to deliver its next update, called Unix System V.4, this summer—a year ahead of the OSF product. "It is definitely a standard," says Eric L. Kim, vice-president of software supplier Ashton-Tate Inc. But that may not mean much. Recently, both sides have quietly adopted ground rules that will minimize differences between their products.

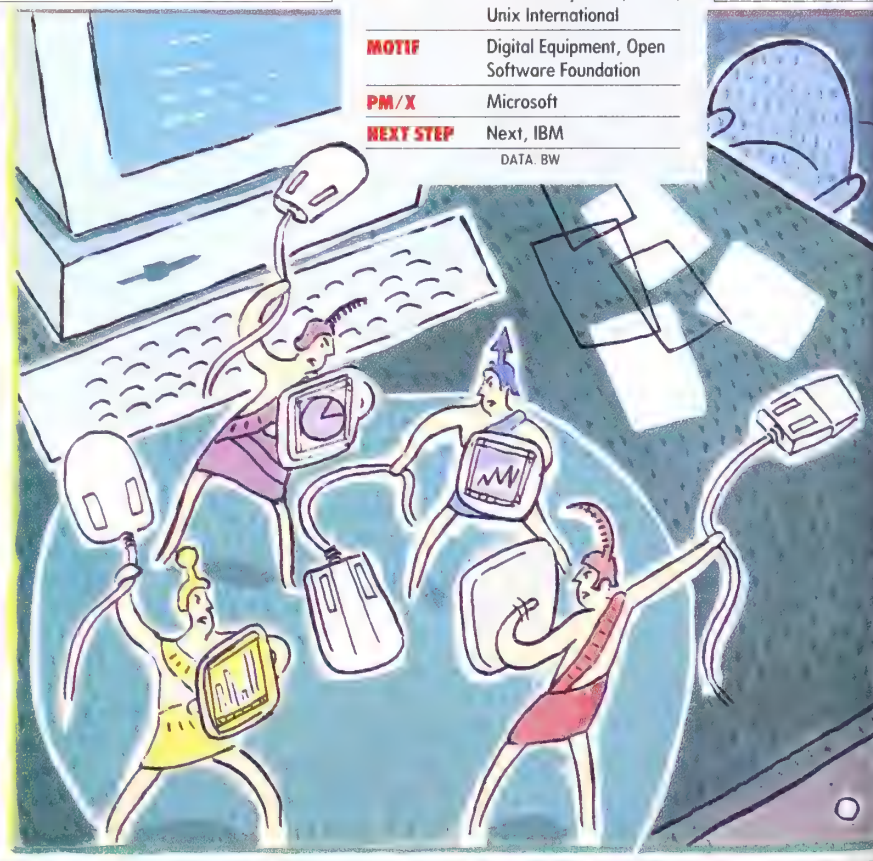
GRAPHICS GAP. Now the competition has shifted to two arcane software features that both versions of Unix must have to muster a popular following. One part, the "graphical user interface," is the means by which man and machine communicate. The other one is a programming interface—it determines how ap-

plications such as spreadsheet programs work with the Unix system. Four main content

THE NEW BATTLE OVER STANDARDS

Product	Principal backers
OPEN LOOK	Sun Microsystems, AT&T, Unix International
MOTIF	Digital Equipment, Open Software Foundation
PM/X	Microsoft
NEXT STEP	Next, IBM

DATA. BW



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ers are vying to be the standard-setter. And until one emerges dominant, software companies are unlikely to write many applications programs for Unix. Unless they do, Unix won't take off in the biggest market—desktop computers.

At the moment, OSF is leading this new race with a graphics program called Motif. It reproduces on Unix the "look and feel" of OS/2, the operating system from Microsoft Corp. that IBM offers with its PS/2 computers. Motif is backed by some influential software makers, including Santa Cruz Operation Inc., the leading seller of Unix for PCs. Santa Cruz' newest product, called Open Desktop, includes Motif and has been endorsed by a half-dozen sellers of IBM-compatible personal computers, including Compaq, Hewlett-Packard—and even AT&T. "Right now, Motif definitely has the lead," says analyst Paul V. Cabbage of Dataquest Inc. SPSS Inc., a Chicago-based software producer, recently polled developers of applications programs for Unix and found that 38% favored Motif.

Still, a series of Byzantine alliances and conflicts makes the race difficult to call. Take AT&T. It has endorsed Open Desktop for PCs. Thus it seems to bless a primary competitor to its own graphics interface, called Open Look, which it developed jointly with Sun Microsystems. Open Look was No. 2 in the SPSS poll.

Microsoft is in an equally bizarre position. It endorses Open Desktop. And its partner, Santa Cruz, plans to convert Microsoft applications for OS/2 to run on Open Desktop. But what Microsoft really wants is to promote OS/2. So it is also pushing its own Unix graphics system, the PM/X, which it says would make converting OS/2 programs to Unix easier.

SPLIT DECISION. And when it comes to labyrinthine logic, don't overlook Big Blue. IBM backs Motif but has also paid \$10 million to license Next Step, a Unix graphics program developed by Steven P. Jobs's startup, Next Inc. Next Step finished fourth in the SPSS survey, but its prospects could change if IBM uses it in new workstations, expected later this year. "We'll probably offer both [Motif and Next Step]," says an IBM spokesman. "We're not an either-or company."

Such confusion arises because each company is hedging its bet. And that continues to slow Unix' progress into mainstream office use from niche markets such as engineering. A few large software companies can afford to work on applications packages for OS/2 plus different versions of Unix. But smaller rivals don't have that luxury. Software Publishing Corp., for example, won't consider Unix now. "It's technically superior to OS/2, but who cares?" says

Fred M. Gibbons, president of Software Publishing. "There's no such thing as standard Unix."

Unix continues to make progress, of course. Last year the fight was over which version to use. Now that seems settled. Unix International's Unix V.4 appears destined to dominate. The OSF system will compete but mainly on large

systems rather than workstations. And in the fast-growing personal computer market, Unix will someday compete with OS/2 to displace MS-DOS, the IBM operating system that now runs 23 million PCs. But when that happens depends on how long it takes for a winner to emerge in the battle of the graphics interfaces.

By Richard Brandt in San Francisco

CAN THIS SMALL FRY PUT UNIX IN A MILLION DESKTOPS?

While industry giants tussle over how to standardize Unix and make it a popular choice for office computers, one unlikely competitor has already built a substantial business on Unix. The company, Santa Cruz Operation Inc., was launched as a father-and-son consulting shop in 1979. The son, Douglas Michels, 35, preferred the Monterey Peninsula to Silicon Valley and vowed to quit if SCO ever grew larger than 30 people. It now has 900 employees and is expected to double its revenues to \$120 million this year. Michels is still there. He's even thinking about a public stock offering.

Long before the Unix wars, SCO was selling Unix systems to customers who couldn't afford minicomputers. Putting Unix on an IBM PC/AT and stringing wires to several \$300 terminals gave a small business a minicomputer-like system at a fraction of the cost. SCO has sold 400,000 such setups.

That prepared SCO for bigger things. Last month it announced Open Desktop, a set of software for IBM compatibles that includes SCO's Unix as well as data-base, graphics, and networking packages. It can also run existing PC software. All this could make Unix much more appealing for use on PCs—especially in large corporations. "We're trying to create a major new market," says Doug Michels, SCO's chief strategist.

BIG RISK. With endorsements from Tandy, AT&T, ComputerLand, and Compaq, Open Desktop looks like the best bet for establishing Unix on PCs. "They have a real potential for payoff," says Paul V. Cabbage, who follows the Unix market for Dataquest Inc.

Still, SCO is taking a big risk. Heavy development spending and the cost of grabbing a one-third share of the Unix market have already squeezed profits. SCO predicts gross margins of only 5% to 10% this year. Some of Michels' fi-

nancial worries were erased in March when Microsoft bought a 20% stake in SCO for an estimated \$25 million. For several years, Microsoft has used SCO to distribute Xenix, its version of Unix for IBM-compatible PCs. Now, SCO is re-writing Microsoft applications packages for Unix and Open Desktop.

The deal puts SCO in an enviable, if awkward, position. Although Microsoft is putting some of its chips on Unix, Chairman William H. Gates III insists

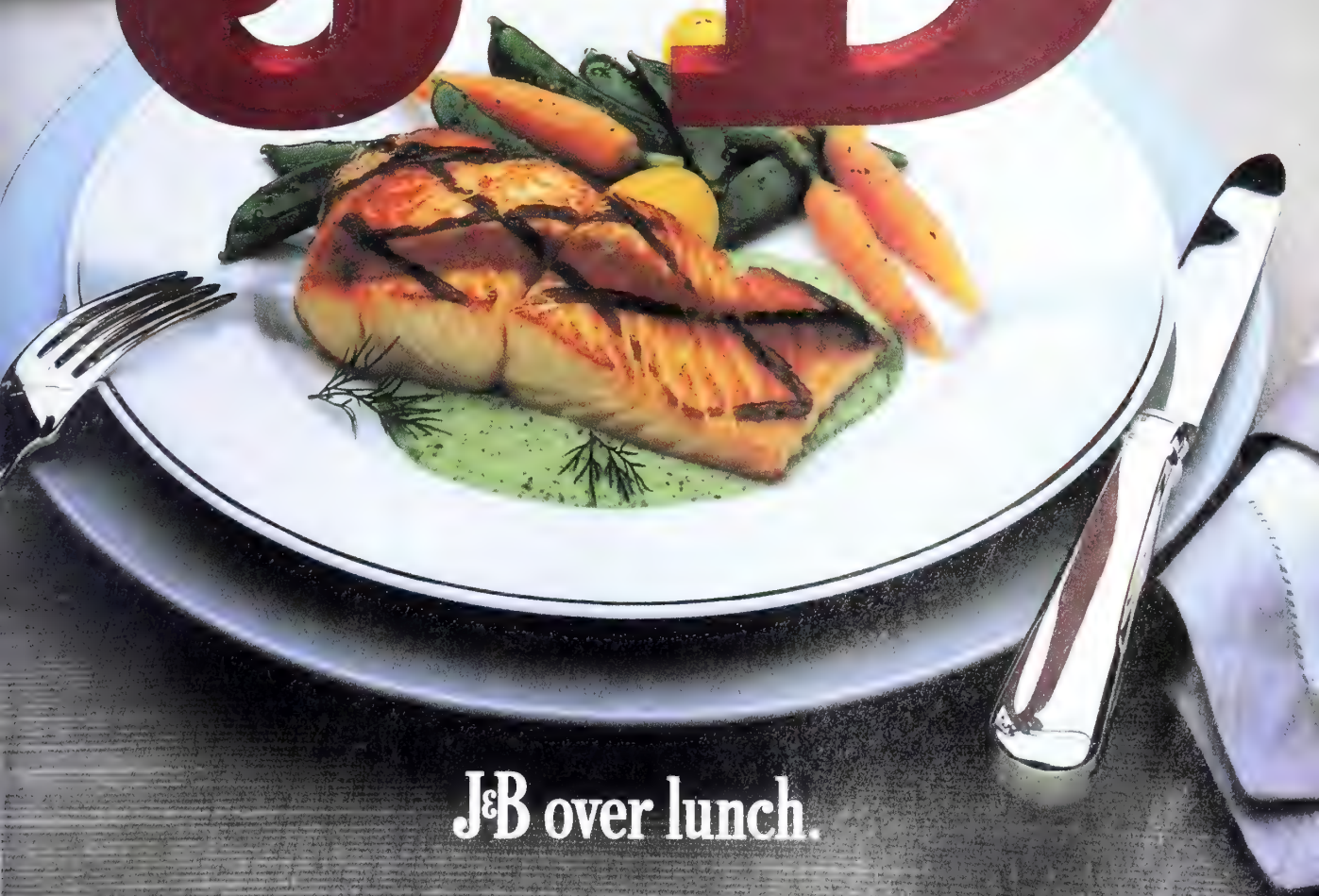


THE MICHELIS: SCO'S FATHER-SON TEAM

OS/2 will be the dominant PC operating system. But Open Desktop could become OS/2's biggest challenger. It's mainly a difference in point of view, says President Larry Michels, 58. Microsoft sees Unix as a small but important slice of the business, while SCO hopes for something a lot bigger. Microsoft's investment at least is a show of unity, says the elder Michels. He likens it to a king marrying off his daughter to a neighboring prince: "I didn't ever stop the wars, but it looked good in the history books."

By Richard Brandt in Santa Cruz, Calif.

J&B



J&B over lunch.

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COMEDY CLUBS CAN BE KNOCKOUTS

Another trip, another meeting, another evening on your own in a strange town. There's nothing funny in that—but there can be. These days, every big city has at least one comedy club—some in cramped basements with hard chairs and cheap beer, a few in glitzy showplaces with champagne on the menu.

Whatever the premises, the promises are the same: fun and laughs as a half-dozen hopeful jokesters take turns at the mike. Many of them rotate from one club to another, and part of the adventure

is that some of the fresh faces you'll see may turn out to be successors to such comedy-club alums as Eddie Murphy and Roseanne Barr.

A handful of upscale clubs—notably Caroline's in Manhattan—offer name performers known from TV appearances with Johnny Carson or David Letterman. Their hefty cover charges and drink minimums can run the tab for an evening's laughs up to \$40 or \$50 per person.

Settle for unknowns at most clubs, and it's \$25 or less—or, as one newcomer said after eyeing the caricatures of famed comedians on the walls of Rags to Riches in New York: "I'm Taylor Mason, someone you can afford."

RUDE SURPRISE? While you'll find more blue jeans than blue suits in many clubs, some are popular sites for corporate celebrations. In Atlanta, for example, McDonnell Douglas Network Systems

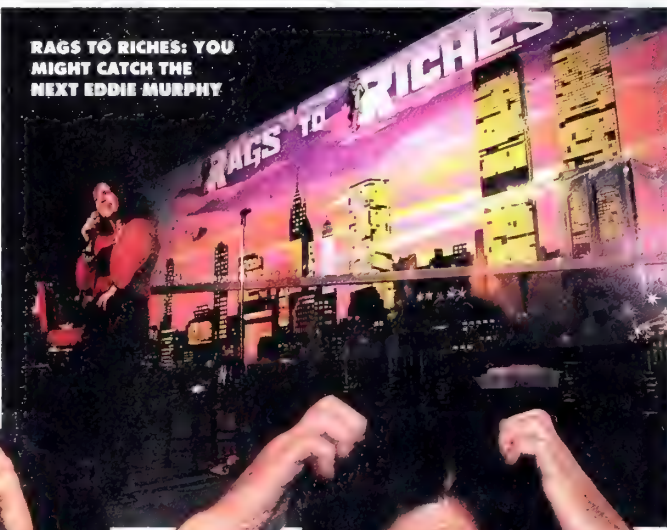
held a Christmas party at the Punch Line, and GE Capital employees went there when the office's lending portfolio topped \$1 billion. "Usually a lot of people beg off" from after-hours functions, says Nancy Ham, assistant vice president. But the club's luck resulted in few no-shows "and people mingled easily."

If you go to see a comedian you like from TV appearances, be warned: The act can be entirely different in a club's freewheeling atmosphere. The raunchy language and confrontational approach of others on the bill can have off-putting effect. At the Comedy Store in Los Angeles, for example, a popular black performer is known for singling out whites who e while he's onstage, verbally attacking them as "trail trash, probably on the way their Winnebagos to eat peanut-butter-and-jelly sandwiches." So, bearing in mind that decorum is seldom a priority, here's a brief guide where the jokes are:

■ **Atlanta.** The seven-year-old Punch Line (404 252-5233) in the northern suburb of Sandy Springs prefaces a veteran headliner with an up-and-coming performer. After an introductory act warms up the crowd, J. Leno was regular in the early years and occasionally drops in to test new gags in the familiar warmth of the room's dark oak beams and hardwood floors.

■ **Boston.** Part of a publicly owned chain of six clubs that grew from a New York City original, the local Catch a R

RAGS TO RICHES: YOU MIGHT CATCH THE NEXT EDDIE MURPHY



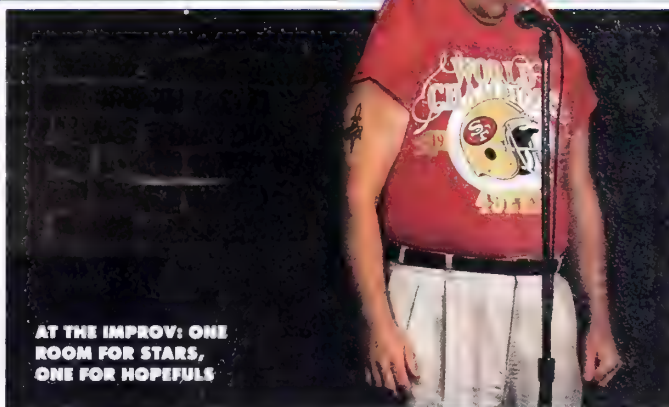
PHOTOGRAPH BY GUNTER WISE FOR W (L) CHLOE SALTHERY FOR R (L)

Star on Harvard Square
Cambridge packs collegians
a small basement room to
ch the better-known comics
sing through town. Reser-
vations are important on
weekends (617 661-9887). At
Riches, a larger and more
comfortable club near Boston
University (254-3939), political
comic Barry Crimmins is
secured on Thursdays.

Denver. Before she hit star-
line with her TV series last
year, Roseanne Barr managed
to make the crowds at the
Comedy Works (303 595-3637)
get the hard plastic chairs
and tiny tables in this down-
town basement room. Show
up 45 minutes early for a
red seat to listen to four or
five comics deliver such lines
as Jim Truman's: "I flew to
Lake City, and the pilot
announced: 'We're about to
land in Utah. Please set your

If you sometimes wish you
had your broker's Quotron
terminal at your elbow but
at paying more than \$200
a month, LiveWire may be
your ticker. Developed by
SoftSoft Inc. (515 472-8393)
Fairfield, Iowa, it's a com-
puter-aided software program
that add-in "board" for any
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computer. The \$995 system
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mated market-watcher and
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picks each new quote from
the FNN ticker and updates a
circular listing of your portfolio.
The program keeps a run-
ning total of 17 days of hour-
ly changes, 136 days of daily
closing positions, and 130
weeks of weekly data. With a
few keystrokes you can gen-
erate technical-analysis and
line graphs to help spot
turning points.



AT THE IMPROV: ONE
ROOM FOR STARS,
ONE FOR HOPEFULS

watches back 2,000 years.'"

■ **Los Angeles.** With walls full
of photos of some 200 comics
who have played there—in-
cluding Robin Williams and
Billy Crystal—the Comedy
Store (213 656-6225) has two
rooms: a smaller one for
newer performers and a larger
one (with a higher cover)
where big names appear on

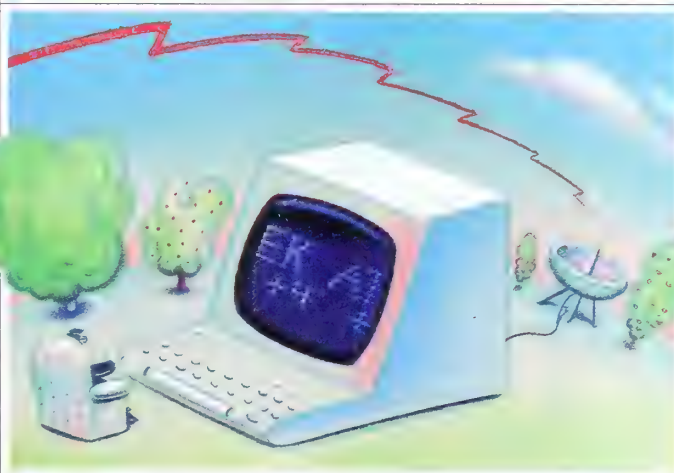
weekends. The Wednesday
night lineup of newcomers
usually offers the best bet for
continuous laughs. The Im-
prov (651-2583) is well-known
via several cable-TV series fea-
turing young performers in-
troduced by Jackie Mason,
Carl Reiner, and other stars.
As many as 15 comics may
appear on a single night, and

you could spot such celebri-
ties as Mike Tyson and Mi-
chael J. Fox in the audience.
In West Los Angeles, the inti-
mate Igby's (477-3553) lets
both established and rising
comics try new gags out of
view of the talent-watchers
who haunt the other places.

■ **New York.** Of a dozen com-
edy clubs in town, Caroline's at
the Seaport (212 393-9400) is
an upscale spot that books a
headliner—Yakov Smirnoff or
Saturday Night Live's Denis
Miller, for instance—who
gets a warmup from a bright
newcomer. The original Catch
a Rising Star on the Upper
East Side (794-1906) packs in a
crowd of youthful profession-
als to watch a half-dozen up-
and-coming performers. More
conveniently located to mid-
town hotels is the new Rags
to Riches on East 54th Street
(688-5577). *Don Dunn*

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can shift LiveWire into the
"background" while you use
the PC for other things, and it
will continue to keep an eye
out for your interests. If, for
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specified stop-loss mark, a
beep and a flashing alert mes-
sage let you know. Press a
"hot key," and LiveWire pops
back onto the screen. Your

other on-screen work then
moves into the background
without your losing any data.
SMOOTH SAILING. Melvin Ver-
non, a vice-president at invest-
ment banker J. C. Bradford's
Danville (Va.) branch, plans to
use LiveWire after he retires
this year: "I'll be able to go
out and play golf, come back,
and see what happened."

Limitations? For one, the
quotes on FNN are delayed by
15 minutes. The ticker doesn't

include some smaller trades
on the New York and Ameri-
can exchanges, and it ignores
over-the-counter transactions
even more. Still, says Vernon,
for the investor who can toler-
ate those shortcomings, "it's
ideal—and cheap."

If you don't fancy being 15
minutes behind the pros, look
into services that let you use
your PC to pull in Wall Street
data on an instant basis. One
"real-time" system, Multex-
Quote from Multex Inc. (212
629-8169), costs \$350 and re-
quires either a special FM-
radio receiver, satellite dish,
or dedicated phone line. An-
other, Lotus Signal (415 571-
1800), costs \$600 for software
and an FM receiver. Both ser-
vices have a monthly fee—
typically \$100 or so, deter-
mined mainly by how many
exchanges you view. But the
portfolio-management soft-
ware of these systems
"doesn't work as smoothly as
LiveWire's," says Rick Bul-
len, a computerized-investing
consultant in Hastings, N. Y.

If you're willing to spend
the money for real-time
quotes and you want
LiveWire's software, stay
tuned. A modified version of
LiveWire that picks up FM radio
signals should be available
this summer. *Otis Port*

Smart Money

YOUR VERY OWN BANKER? IT COULD BE TIME

Not long ago private banking was strictly for the white-shoe set. Inheritors of accumulated wealth relied on such old-line bankers as Bessemer Trust and Morgan Guaranty to make sure the family's capital didn't erode and the children received the dividend checks from their trust funds on time.

Today private banking is no longer exclusively for old money. In the past 20 years, large commercial banks have realized that private banking is a lucrative endeavor, and they are aggressively peddling it to those with "created" rather than inherited wealth. If you earn \$250,000 or more, such institutions as Citibank, Chase Manhattan, Bank of America, and others may be eager to offer you

Big banks are selling their private services aggressively

the perks of private banking—for a price.

Private banking entails paying your banker an annual fee—usually 1% of your portfolio's value. That's about the same as a money manager gets. But there may be advantages. "With a private banker, you can use your portfolio as collateral for a personal loan," says Stephen Timbers, chief operating officer at Kemper Financial Services and a former private banking executive at Chemical Bank.

Despite their image as underperformers, the retail banks' equity and fixed-income funds have done as well as, and sometimes better than, those run by other money managers. CDA Investment Technologies (301

975-3600) in Rockville, Md., found that the annualized rate of return over the past five years for bank equity funds was 14.5%. That's better than the 13.6% for investment advisers and 12% for mutual funds.

'CARRY ME.' The watchwords of private banking are confidentiality, customized service, and large loans in short order. So a private banker, working with a staff of attorneys and accountants, will prepare your tax returns, pay bills, write your will, provide secured and unsecured personal loans quickly, manage your stock portfolio, and even manage your estate after you're gone.

The fees for asset management tend to be standard at all the banks—1% on the first \$1 million, ¾ of 1% on the next \$4 million, and ½ of 1% on everything over \$5 million. Some of the old-line banks have high barriers to entry. Bessemer and Morgan prefer clients whose investable assets exceed \$5 million. But Chase, Chemical, and Boston Safe Deposit—a unit of American Express—look for clients with net worths of \$1 million and \$250,000 in annual income. "We like people who need lifestyle financing, which means: 'Carry me over until I get my bonus payment,'" says Chase's Leslie Bains.

The best aspect of private banking, however, is that the bankers pride themselves on being so familiar with your financial resources that they can answer your credit requests immediately. "We'll tailor the loan to the customer," says Rick Gilbert, head of private banking at Citibank. "We don't question [the reason] provided it's not illegal, immoral, or unethical, and we can make money on it." *Laura Zinn*



CLEO LAINE: BEWITCHING INTERPRETATIONS OF DISTINCTIVE SONGS

Recordings

TWO NEW SIDES WHERE SONDHEIM SHINES

In moving from Broadway to the stages of such cities as Los Angeles, Cleveland, and Dallas, Stephen Sondheim's *Into the Woods* has taken on Cleo Laine in the central role of the witch. Evidence of how good a match this is can be found in *Cleo Sings Sondheim* (RCA).

It's as if Sondheim were what Laine had always been waiting for, and vice versa. With his cool observations on human nature, Sondheim sounds a distinctive note in American songwriting, and Laine may be the finest interpretive actress among today's singers, at home with jazz, operetta, and Broadway. Among her featured themes: endurance (*I'm Still Here*), indulgence (*The Ladies Who Lunch*), and the shared insecurity of children and parents (*No One Is Alone*). They're enhanced by Jonathan Tunick's sensitive orchestrations.

REEDY TENOR. For a fine male interpretation of Sondheim's music, there's *Mandy Patinkin* (Columbia), the singer/actor's first solo album. Patinkin earned his Sondheim credentials with his lead role in *Sunday in the Park with George*. And the four Sondheim songs are miniature masterpieces: They display a clear sense of intent and the impeccable, knowing exe-

cution of a fine actor.

But the record's 12 other tracks are another story. Patinkin's reedy tenor does wear well over the hour length of the CD. Away from the structures of Sondheim, Patinkin doesn't seem to know when to rein in the emotion and just sing the notes. His *Soliloquy* (from *Carousel*) is overloaded with gestures—which end up conveying less meaning than Sondheim's. *Ray Hoffman*

Worth Noting

■ **SOUTHERN SPRING.** About 100 of Charleston's fine 18th and 19th century homes and gardens are on display through Apr. 11. Proceeds from the three-hour, \$25 walking tours, which run at 10 a.m. and 2 p.m., benefit the Historic Charleston Foundation. For tickets, call 803 722-3405.

■ **PENSION POINTERS.** Everything small-business owners ever wanted to know about Simplified Employee Pension Plans can be found free in Labor Dept. booklet. Write SEPS, Room N-5666, 200 Constitution Ave. NW, Washington, D.C. 20210. Self-addressed, stamped envelope are "appreciated."



*“Feel
the great forces
that are behind
every detail.”*

—Oliver Wendell Holmes

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From small key systems to digital PBX, nearly two million American business people depend on Toshiba reliability to stay in touch.

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TOSHIBA BUSINESS TELEPHONE SYSTEMS

In Touch with Tomorrow
TOSHIBA



POISED FOR THE 90's THE RE-MAKING OF AMERICAN MANUFACTURING



Primed to compete, U.S. manufacturers are in a global footrace for the future.

It is the quintessential American machine... and success story turned sour.

In the eighty-plus years since Bill Harley and the Davidson brothers rolled their first production motorcycle out of a ten by fifteen foot shed-turned-factory, the road machine born in the backyard of the Milwaukee mechanics has come to symbolize the raw power of American ingenuity, craftsmanship, and confidence in tomorrow.

For almost seven decades, the "Harley" reigned King of the Road. It was shot at in two World Wars, chased Bonnie and Clyde, and carried Peter Fonda and an entire generation through the turmoil of the 60's.

Then Harley went into a sudden stall, its engine overheated by rapid growth and

POISED FOR THE 90'S THE RE-MAKING OF AMERICAN MANUFACTURING

inattention to quality that can come with it, intense competition from abroad, and fall-out from what Eastman Kodak Chairman and CEO Colby H. Chandler recently described as "an experiment in national economic policy which brought both great benefit and harm to the U.S. economy."

"The benefits: the taming of inflation and the longest peacetime expansion of this century."

The harm: the largest budget and trade deficits in our history. And the steady erosion of U.S. manufacturing's competitive stature and edge.

"Things looked pretty grim," concedes National Association of Manufacturers (NAM) President Alexander (Sandy) Trowbridge. "The high dollar, combined with a sense of complacency on the part of U.S. manufacturers, translated into lost markets here and abroad."

Today, Harley Davidson—along with major players in the domestic steel, automotive, and other key manufacturing sectors—is not only back on the road but burning it up. Costs are down, quality is up, and thanks to a more realistically valued dollar, American-made goods are gaining ground in foreign markets.

Here at home, the naysayers, who not only predicted but welcomed the coming of a post-industrial, service-based, manufacturing-less economy, are uncharacteristically quiet. But, the race is just beginning.

"American manufacturing is definitely on the upswing," observes Trowbridge. "A quarter of NAM's board of directors, in a

recent survey, said they now have a competitive edge on foreign competition. Sixty-one percent say they're holding their own."

"But, we won't get complacent again. There's still a long way to go to regain our competitiveness...and a lot of roadblocks."

[Manufacturing] puts the 'smart' in smart machines, heartbeat in electronic pacemakers, and lift in everything from elevators to booster rockets.

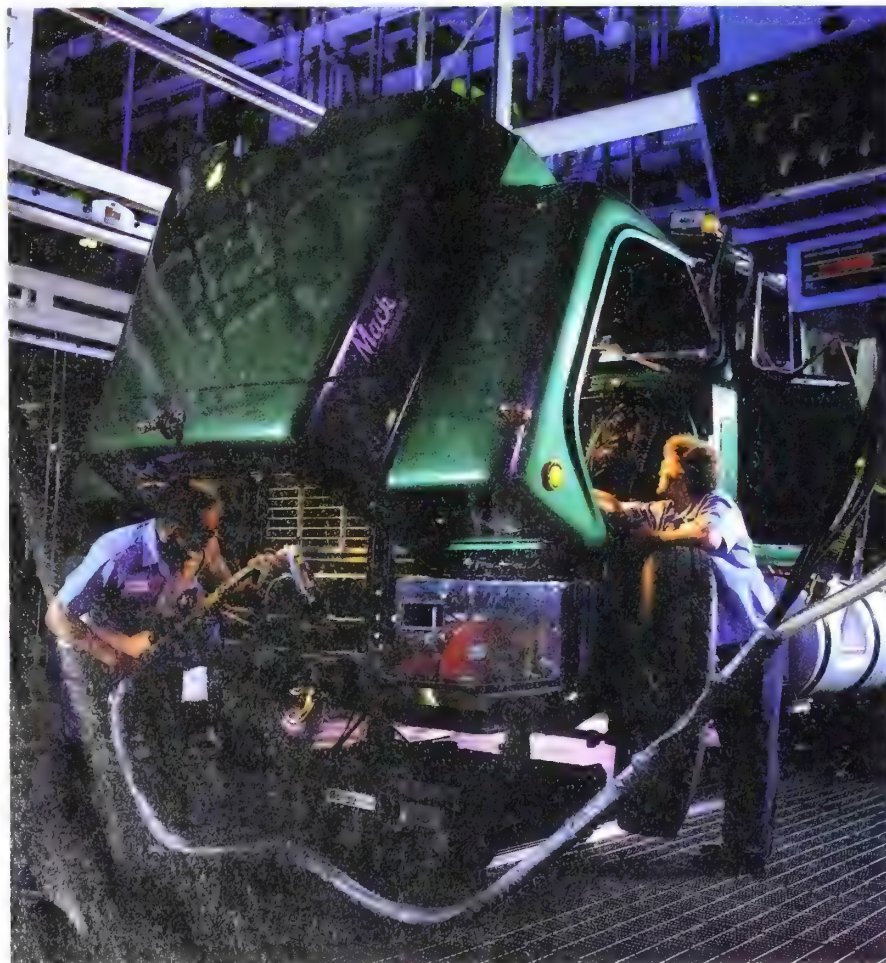
A Mandate To Make

If the increasingly high-tech smokestacks of American manufacturing fail to stand up to intense global competition or collapse inward under the weight of misguided, national macroeconomic policies, and/or managerial ineptitude, the fallout will be far-reaching. Dust will settle on the American Dream.

From the introduction of the Wilkinson lathe, patented in 1798, to the electronic entrepreneurship of Silicon Valley, manufacturing has spurred and underwritten both the growth of the U.S. economy and a progressively higher standard of living. Pay-check for paycheck, manufacturing jobs pay 20 percent more than non-manufacturing jobs and nearly 30 percent more than service sector jobs.

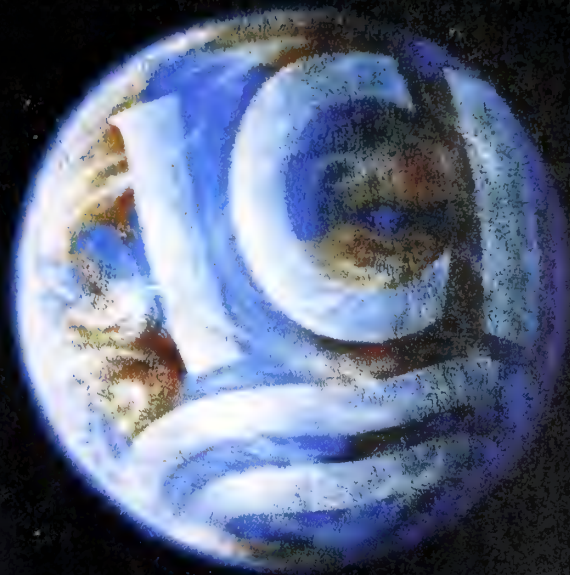
Although manufacturing's primary mission is to make, the sector is also a powerful magnet for the output of other industries. "In 1986, manufacturing directly contributed over one-fifth of America's gross national product, yet shipments by manufacturing companies equaled almost 60 percent of the GNP," MIT economists Rudinger Dornbusch and James Poterba, and Harvard's Lawrence Summers point out in a recent report commissioned by Eastman Kodak titled, "The Case For Manufacturing In America's Future." "Equaling nearly 40 percent of the GNP, the difference reveals the extent," they note, "of manufacturing's purchases from other sectors of the economy."

Manufacturing is no less important a player in the international trade and debt arenas...important but bloodied in recent



Mack Trucks emphasizes quality control. Above: Workers perform final checks at the end of assembly loop.

COURTESY OF MACK TRUCKS



Discover who we are, and you will think the world of us.

The fact that we are the fourth-largest chemical company in the world with global sales of \$21 billion (\$4 billion in the U.S.) may have escaped your notice. This is an effort to change that.

We make the world a little safer.

In the immediate future driving cars will be safer, because airbags actuated and inflated by components from ICI will inflate in 4/100ths of a second to protect the front-seat occupants.

Today, criminals can more accurately be tied to their crimes through high-tech DNA FINGERPRINTING™ which our Cellmark Diagnostics business is pioneering.

Innovative waterborne coatings introduced by ICI's Glidden reduce dependence on atmosphere-polluting alternatives.

We make the world a little healthier.

1.5 million people suffering from hypertension in the U.S. control it with the first one-tablet-a-day beta blocker, which we manufacture.

We discovered the leading oral medication for advanced and post-surgical treatment of breast cancer.

Mylanta® and Mylanta-II are used by more than 12.7 million adults each year in the United States.

We make the world more durable.

Thoro products have waterproofed and protected the Tower of London and the observatory at

Mt. Washington, New Hampshire.

One out of every two cars manufactured in the United States is built using Molub-Alloy® or Tribol® lubricants supplied by ICI's Tribol.

We make the world more beautiful.

We are the world's largest maker of paint and make enough annually to cover 10 million homes.

America's fashion designers choose our Tactel® textile fiber for apparel ranging from fine hosiery to weather-tough skiwear.

We lead North America in supplying ink for snack food and confectionery packaging.

We make the world more efficient.

We have the fastest-growing agrochemical business in the United States.

Worldwide, we are the third-largest producer of crop-protection chemicals and the fourth-largest agricultural products company in the U.S.

We help to store and retrieve the world's information more effectively by providing Melinex® film base.

We are at the leading edge of polyurethanes technology, contributing significantly to the U.S. automotive parts, recreational footwear and construction markets.

At ICI we bring a lot to the world. And we are about to bring much more.

World Problems World Solutions



World Class

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*"American manufacturing
is definitely on the
upswing," observes (NAM)
President Alexander
(Sandy) Troubridge.*

of the country's almost \$800 billion
defense budget.

Global Ambitions

Foreign manufacturers are not
waiting for the U.S. economy to
recover. They are already moving in.

world's largest markets which, after the
collapse of the Soviet Union, are
fast becoming the new mega trading
areas. These are called the Triad: Japan,
North America, the United Kingdom, and
the United States of America.

The Triad are joined by agreements
regarding free trade. These agreements
are designed to allow trading patterns to
develop between the United States, Japan,
Canada, U.S. Trade Agreements and America
in 1992; European Community Internal
Market Program.

In the meantime, Japan, Korea, Taiwan,
China, Hong Kong, and Singapore
are also becoming major trading partners.
These are the so-called Four Tigers. South
Korea, Taiwan, Hong Kong, and Singapore
are also becoming major trading partners.
These are the so-called Four Tigers.

major market. Through the
free trade treaties of the Triad
trade with the other two
countries is an annual total
of \$100 billion. This figure is
expected to rise to \$200 billion
by the year 2000.

A shared strategy: global-
ization gives the major
powers a world market that
access to each other's
markets. Through these
treaties, the major powers
are able to exploit their
commercial exploitation
of each other's resources
in the development of
new technologies.

Where does that leave U.S.
manufacturers? The answer
is simple. The U.S. is the
most powerful in a just issued
report titled "Remaining
The American Dream: Risk
Policies For A Competitive
Nation."

Although the U.S. is the
most powerful in the world,
it is not the most powerful
in the Triad. The U.S. is
the most powerful in the
Triad, but it is not the most
powerful in the Triad. The
U.S. is the most powerful in
the Triad, but it is not the
most powerful in the Triad.



Chemicals manufactured in this Eastman Kodak plant in Tennessee have applications in food, photographic and rubber products.

factoring in a twenty-four-

hour operation. The plant

handles 200,000 gallons of

A NEW DIMENSION

ck® CH600. Technology takes a quantum leap in the first new truck designed for '90s. And beyond. It's a new dimension in room, comfort and performance for heavy-duty highway hauling. Every inch built with *Balanced Design*, from its totally new chassis and cab to its integrated sleepers and unified aerodynamics. See the 600 at your Mack dealer. It's not just a new shape. It's a whole new dimension.



MACK QUALITY
Depend on it!

\$1,153,278

600,000

(and more) makes Chase #1 in
information and
transactional services.

Over a trillion dollars.

That's the amount of money our clients entrust to our
information and transactional services division on an
average day.

\$834,029,200,000 in trust and securities services alone.
\$316,578,300,000 in daily payments. \$2,671,100,000 in trade
transactions.

Obviously, this volume of transactions represents a very
significant part of our business.

Which is why we're now giving this division of Chase a
title worthy of its importance: Chase InfoServ International.

The fact is, Chase InfoServ International is already a
leader in virtually every type of information and transactional
service to corporations and institutions around the world.

But we know it takes more than big numbers to be #1.

It takes consistently reliable service.

It takes fast, accurate reporting.

It takes state-of-the-art technology.

Admittedly, big numbers are an effective way to show the
size of the Chase InfoServ commitment.

But we know that leadership depends on a genuine and
ongoing interest in your problems and needs every day we do
business with you.

Chase InfoServ International: Cash Management / Payments / Collections /
Trade Services / Global Electronic Banking / Master Trust / Global Custody /
Public Pensions / Corporate Trust / Stock Transfer / Municipal Agent

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POISED FOR THE 90's THE RE-MAKING OF AMERICAN MANUFACTURING

budget that ballooned to 4.2 percent of GNP in the 1980's, net national saving—the sum of individual and corporate saving, plus government surpluses or deficits—tumbled to two percent of GNP.

"That rate is about one-third the U.S. average of the 70's and one-fifth the current average of the major industrialized countries," notes Hewlett-Packard President and CEO and Council on Competitiveness Chairman John A. Young. "And it's far too low to finance the levels of domestic investment needed to bolster American competitiveness. Given that U.S. investment has fallen to a post-war low in the 80's—down to 4.8 percent of GNP," Young adds, "other countries could soon surpass America's productivity performance."

Foreign manufacturers have made giant strides in closing the one-time gaping productivity gap. Between 1960 and 1979, U.S. productivity grew at only one-third the rate charted by Japan.

American manufacturers did not fare much better in the exports arena. In the 15-year period 1970 to 1986, U.S. exports grew at an annual rate three percent below that of other industrialized nations. By most yardsticks and with the world watching, U.S. manufacturing was in deep, some said irreversible, retreat.

Back On Track

On their backs and being written off as dinosaurs from Wall Street to Washington, American manufacturers skirted but did not fall into the abyss. To the contrary, by late last

year quality was up, costs were down, and economists and the business press were heralding the comeback of U.S. manufacturing.

"The most pervasive and powerful reason for this improvement is the depreciation of the dollar relative to the currencies of our major trading partners," says NAM's Jasinowski. "The first stage of manufacturing's drive to become more globally competitive succeeded through a 40 percent exchange rate improvement and ten to 25 percent reduction in business costs. On a ten-point scale, U.S. manufacturing is now at '4' and climbing."

Although the devalued dollar has played a key role in helping return U.S. manufacturing to competitiveness, credit for the revival

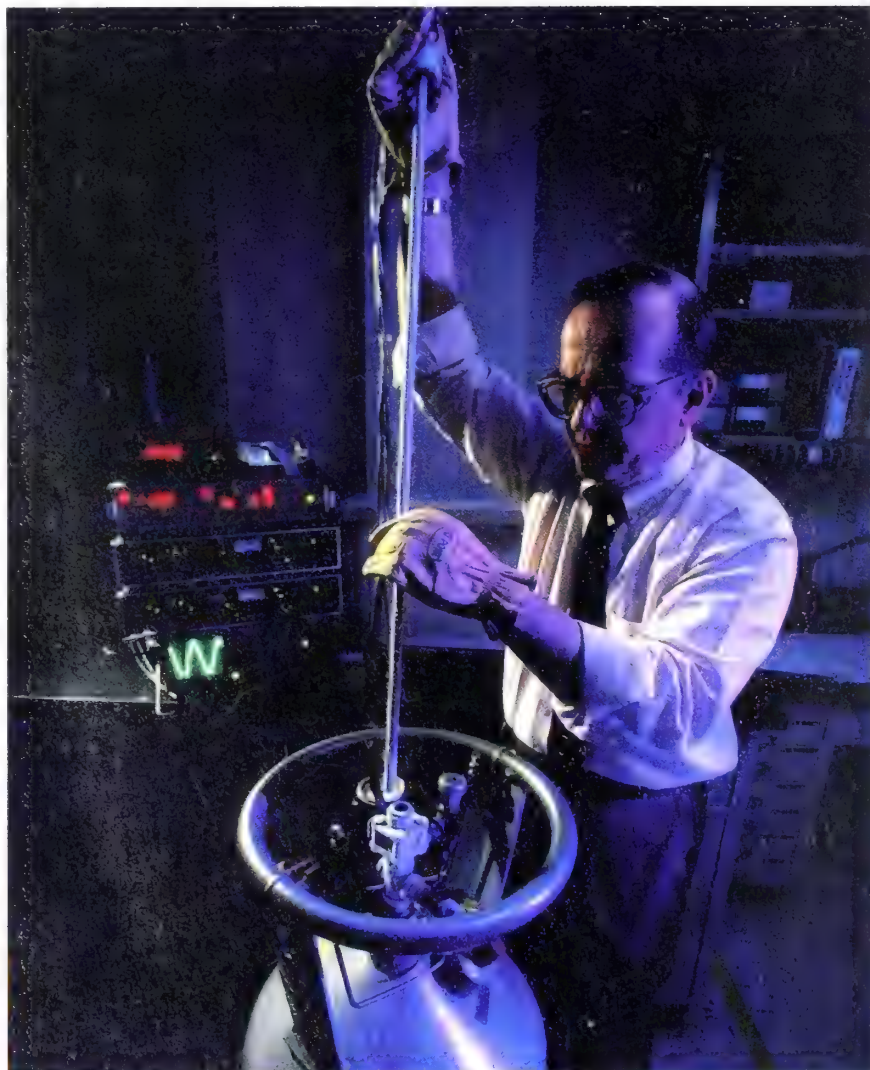
also goes to a range of rigorous, self-help measures—rampant restructuring, downsizing, the layering of management, and a renewed emphasis on quality, employee participation, and cost control techniques—implemented by domestic manufacturers during the early 80's.

Being driven off the road by Honda, Kawasaki, Suzuki, and Yamaha, Harley-Davidson launched an ambitious revitalization program incorporating many of the techniques used by its Japanese competitors. As a result, the motorcycle maker was among the first American companies to institute Just-In-Time (JIT) inventory control, statistical process control (SPC), and employee involvement.



The Goodyear Cereal Food Processors Mill in Cleveland, Ohio, produces 850,000 pounds of flour daily.

COURTESY OF GOODYEAR



Recent research and development at Du Pont led to the discovery of a new higher-temperature superconductor.

*For Bill Demby, the difference means
getting another shot.*



When Bill Demby was in Vietnam, he
used to dream of coming home and play-
ing a little basketball with the guys.
A dream that all but died when he lost
both his legs to a Viet Cong rocket.

But then, a group of researchers dis-
covered that a remarkable Du Pont plastic
could help make artificial limbs that were
more resilient, more flexible, more like
life itself.

Thanks to these efforts, Bill Demby

is back. And some say, he hasn't lost a
step.

At Du Pont, we make the things that
make a difference.

Better things for better living.



Snap-on. Tooled-up for America's future.



Snap-on

NUMBER ONE SINCE 1920

...there is a difference

SC 19

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The payoff? In less than a year, JIT saved Harley more than \$22 million in the form of reduced in-process inventory. And since 1981, productivity has increased nearly 50 percent, manufacturing errors are down 70 percent, and plants are operating with two-thirds less inventory.

In touch with itself and the realities of a changing marketplace, Motorola Inc., launched an ambitious drive, in 1981, to effect a tenfold improvement in its products and services. Five years later, the Schaumburg, Ill.-based manufacturer of two-way radio communications systems, car telephone systems and telephones, modems, and semiconductors had not only surpassed those goals but was busy chasing an even more challenging set of objectives: a tenfold improvement in quality in two years and 100-fold in four years, on the way to achieving what President and CEO George Fisher describes as "Six Sigma" by 1992. "In statistical terms," Fisher explains, "Six Sigma translates into 99.9997 percent perfect product or service."

And that translates into some very impressive real world results. Today, Motorola, the 1988 winner of the Malcolm Baldrige National Quality Award, claims the

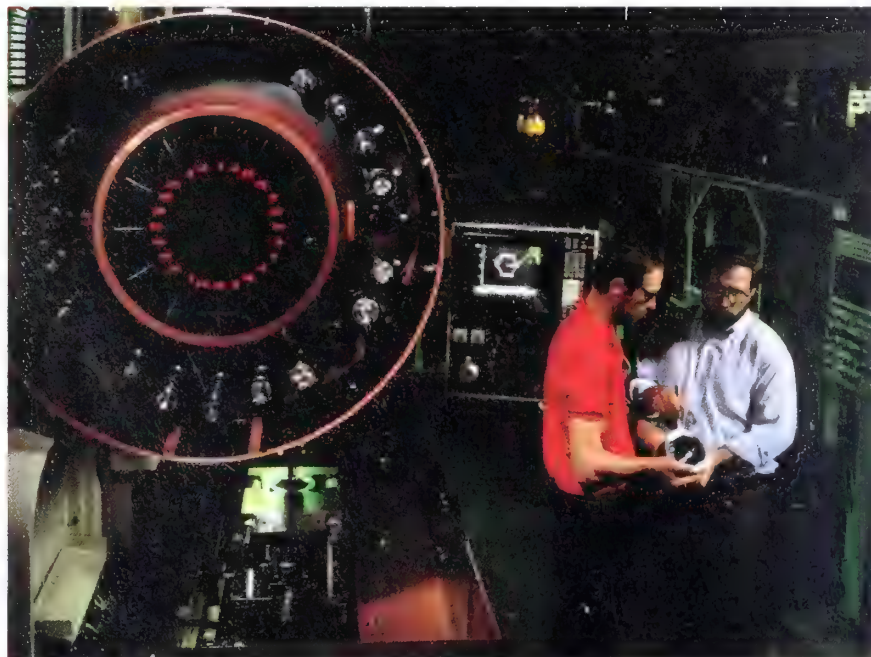
highest annual share of the pocket pager market in Japan and remains the only non-Japanese company to supply pagers to Nippon Telephone and Telegraph.

Since 1970, the productivity growth rate for manufacturing has averaged 3.5 percent. At 0.3 percent, non-manufacturing lags far behind.

In Columbus, Ohio, the home of Worthington Industries, Inc., Chairman & CEO John H. McConnell, who founded the company in 1955 with a single order and \$600 borrowed against the family car, now heads a \$900 million business built on a simple philosophy: Treat customers, employees, investors and suppliers as you would like to be treated.

Worthington, a major processor of flat-rolled steel, is the 370th largest industrial company in the U.S. But its five-year average return on equity of 19.7 percent ranks the company a solid number one in the steel industry for the eighth consecutive year.

Behind those numbers is a tenacious commitment to quality—customer acceptance



Computer-driven machining centers and the cellular manufacturing approach have become important elements in Snap-on Tools Corporation's efforts to improve both product quality and customer service.



Don't listen so much
to what "they" say.
Let your imagination soar.

GOODYEAR

POISED FOR THE 90's THE RE-MAKING OF AMERICAN MANUFACTURING



The effectiveness of herbicide on rice plants is monitored at Du Pont's Stine Laboratories. The company is funding R&D programs to remain competitive.

rate has historically exceeded 99 percent — and an operating philosophy that puts a premium on clear communication, employee involvement, and investing in the future.

Poised For The 90's

Boosted by the depreciation of the dollar, belt-tightening from the tool room to the board room, and re-adoption of quality as a core corporate value, American manufacturing is back.

Will it stay there? More importantly, what will it take to keep U.S. manufacturers on the cutting edge of global competitiveness through the 90's?

Competitiveness begins with wanting to win. To win, American manufacturers must not only re-double efforts to attain and sustain "manufacturing excellence" — being the best at what you do and make by fostering a corporate culture committed to continuous learning and improvement — but reach beyond the factory walls and enlist the cooperation of government and society as a whole to hold on to the American Dream. And Government and society must reach back.

On the corporate front, manufacturers must:

- Build on their recent success and commit to realizing the concept of manufacturing excellence. Investment in research and

development must be stepped up and new technologies wheeled out of the country's laboratories and onto its plant floors faster than ever.

Cooperative generic research should be viewed as not only a catalyst for speeding the commercialization of breakthrough American-born technologies, but a whetstone for world competitiveness.

- Recognize human capital is the cornerstone of manufacturing and economic ascendance. And treat it that way.

Greater emphasis must be put on employee training and re-training and upgrading the nation's education system to insure the availability of skilled workers. Once on the manufacturing floor, workers must be given a strong voice in devising and revising programs to increase quality and productivity. And they must be motivated and re-motivated by compensation systems that relate paychecks to productivity.

On the legislative front, the nation's leaders must:

- Create an environment that supports the competitiveness of American products in the global trading arena. Foreign markets must be opened to American-made goods and the producers of those goods protected from unfair trade practices. Export disincentives must be eliminated and exchange rates keyed to reflect competitive funda-

mentals and prevented from ever again pricing American-made goods out of foreign markets.

- Help coordinate and encourage technology initiatives by maintaining a stable tax policy tooled to promote higher levels of research and development. Regulatory red-tape and obstacles slowing the commercialization of new technologies must be systematically removed.

- Accelerate the adoption of advanced manufacturing technologies by modifying federal tax laws to encourage, instead of discriminate against, capital investment and personal savings. Lower capital gains taxes, restoration of some form of investment credit, increased incentives for savings, and elimination of the double taxation of corporate earnings paid as dividends are key to future competitiveness.

Finally, as a society, America's corporate leaders, shareholders, and employees, Washington, and the electorate it's there to serve must pool their strengths, practice good sense, and stop the joy ride that threatens to wreck our national future. America has got to start living within its means and stop gutting its economic engine room by amassing unprecedented levels of individual, corporate, and federal debt and opting for quick fixes and short-term gains at the expense of its future.

Government must take the lead by holding the overall growth rate of federal spending below the rate of inflation without raising taxes or shifting social costs to employers under the guise of mandated employee benefits. Major regulatory or economic policies should be adopted only after their economic impact on U.S. manufacturing competitiveness is fully assessed. And the nation's securities, financial, and anti-trust laws should be judiciously applied to reinstate the value of a longer-term view.

Taken together, these policies and U.S. manufacturers' own initiatives must do nothing short of remaking America's future. If the recent past in the manufacturing sector is any measure, there is cause for confidence.

This special advertising section was sponsored by the National Association of Manufacturers. For more information, call: 202-637-3000.

The text of this special advertising section was written by Jo Isenberg-O'Loughlin

COURTESY OF DU PONT

You used to hate it when he told you what to do.
Now sometimes you wish he would.



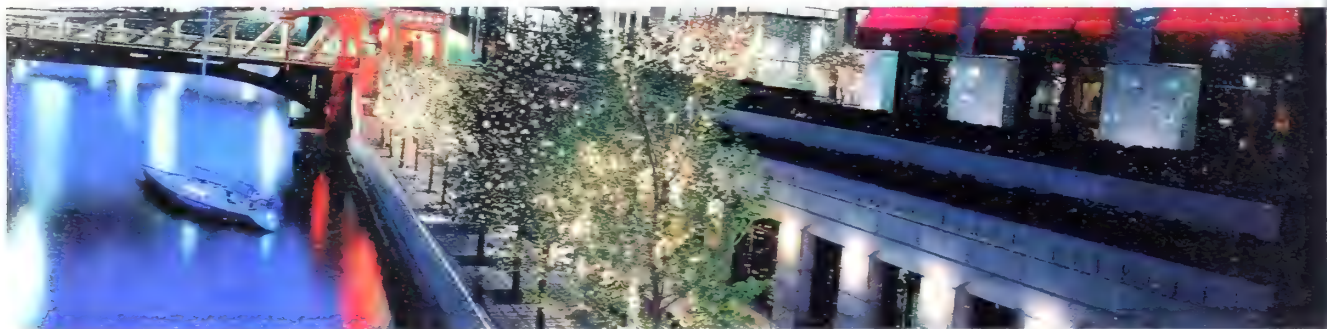
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from one Nikko hotel to another, you can count on some things that will never



change: Facilities, amenities and locations carefully planned to offer you..

Simply everything. Simply.



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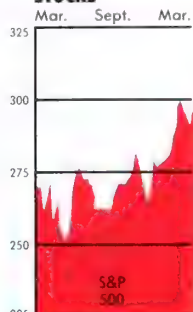
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Investment Figures of the Week

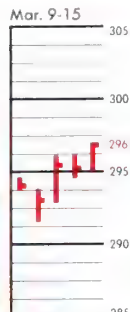
MARKET COMMENTARY

Financial markets meandered, but investors remained concerned about economic tidings. One high of the week was a reported reviving of the nation's trade deficit in January. That sustained stock market on Mar. 15. A rise in crude oil prices, to the highest level in 16 months, sent oil stocks higher. But bond prices were hurt by the news. The technical indicators struck a positive note, as the put-call ratio of speculative sentiment turned neutral had been negative.

STOCKS

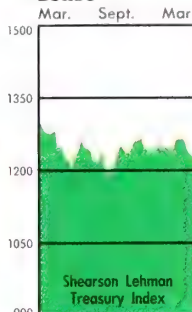


52-week change
+10.4%

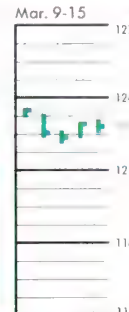


1-week change
+0.9%

BONDS

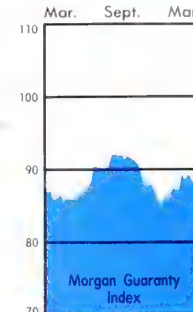


52-week change
-4.8%



1-week change
-0.6%

THE DOLLAR



52-week change
+3.6%



1-week change
+0.4%

MARKET ANALYSIS

STOCKS

	Latest	% change	
		Week	52-week
DOW JONES INDUSTRIALS	2320.5	1.1	12.4
DOW COMPANIES (Russell 1000)	156.9	0.7	10.3
DOW COMPANIES (Russell 2000)	158.3	0.3	11.6
DOW COMPANIES (Russell 3000)	168.5	0.7	10.4

HIGH STOCKS

	Latest	% change (local currency)	
		Week	52-week
DOW (FINANCIAL TIMES 100)	2121.2	1.8	16.2
DOW (NIKKEI INDEX)	32,100.5	0.8	24.9
DOW (TSE COMPOSITE)	3622.2	-0.3	9.7

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	8.7%	8.6%	5.6%
30-YEAR TREASURY BOND YIELD	9.1%	9.1%	8.6%
S&P 500 DIVIDEND YIELD	3.4%	3.4%	3.3%
S&P 500 PRICE/EARNINGS RATIO	11.9	11.9	15.5

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 26-week moving average	280.7	279.6	Positive
Stocks above 26-week moving average	63.0%	61.7%	Neutral
Speculative sentiment: Put/call ratio	0.26	0.24	Neutral
Insider sentiment: Vickers sell/buy ratio	1.11	1.14	Positive

INDUSTRY GROUPS

4-WEEK LEADERS

	% change	
	4-week	52-week
TECHNOLOGY	14.4	39.1
ENTERTAINMENT	10.3	30.4
WELL EQUIPMENT AND SERVICES	7.6	-1.7
DOMESTIC OIL	6.3	4.8
MINING	5.7	-29.2

4-WEEK LAGGARDS

	% change	
	4-week	52-week
VEHICLES	-7.4	14.6
FREIGHT	-6.2	13.4
INSTRUMENTATION	-5.4	-9.9
COMPUTER SYSTEMS	-5.3	-3.8
PACKAGING	-5.2	-1.2

Strongest stock in group

	% change		Price
	4-week	52-week	
TONKA	38.7	22.4	13
WARNER COMMUNICATIONS	24.3	56.3	49 3/4
BAKER HUGHES	14.5	-4.3	16 3/4
AMERADA HESS	13.3	19.8	36 1/4
GENESCO	14.0	36.1	6 1/8

Weakest stock in group

	% change		Price
	4-week	52-week	
CHRYSLER	-9.3	4.6	25 5/8
FEDERAL EXPRESS	-6.4	9.6	49 3/4
HEWLETT-PACKARD	-6.0	-12.2	54 5/8
INTERGRAPH	-24.7	-42.6	16
CONSOLIDATED FREIGHTWAYS	-10.3	-2.5	29 1/2

BRIDGE INFORMATION SYSTEMS INC.

MUTUAL FUNDS

LEADERS

	4-week total return	%
STRATEGIC INVESTMENTS	14.3	
UNITED SERVICES GOLD SHARES	12.6	
MAN CAPITAL	7.3	

	52-week total return	%
JFMANN	58.0	
UMBRIA SPECIAL	36.5	
TEL CAPITAL APPRECIATION	36.2	

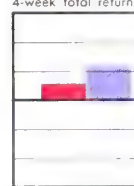
LAGGARDS

	4-week total return	%
MERRILL LYNCH PACIFIC	-5.9	
NOMURA PACIFIC BASIN	-4.9	
FIDELITY PACIFIC BASIN	-4.9	

	52-week total return	%
STRATEGIC INVESTMENTS	-22.6	
STEADMAN OCEANOGRAPHIC TECHNOLOGY	-19.0	
UNITED SERVICES GOLD SHARES	-15.5	

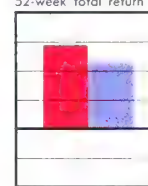
S&P 500

4-week total return



Average fund

52-week total return



RELATIVE PORTFOLIOS

Amounts represent the present value of \$10,000 invested one year in each portfolio

Figures indicate yearly total returns

	Foreign stocks	U. S. stocks	Money market fund	Treasury bonds	Gold
Amount	\$12,472	\$11,390	\$10,650	\$10,300	\$8,941
Return	-1.06%	+0.43%	+0.16%	-0.42%	+1.09%

DATA RESOURCES INC.

Figures on this page are as of market close Wednesday, Mar. 15, 1989, unless otherwise indicated. Relative portfolios are valued as of Mar. 14. A more detailed explanation of this page is available on request.

Mar. 14. Mutual fund returns are as of Mar. 10. Relative portfolios are valued as of Mar. 14. A more detailed explanation of this page is available on request.

BIG IS NO SUBSTITUTE FOR SMART

All the attention on global competition is encouraging a foolish idea: that a company must be big to compete effectively against foreign rivals. That argument was used in the recent merger deal hatched between Time Inc. and Warner Communications Inc. Too many corporate executives buy the bigger-is-better logic.

The issue is not whether companies should be bigger or smaller, but how they should be managed (page 84). Bigness in and of itself is neither good nor bad, and, of course, bigness has important advantages: economies of scale, effective distribution, and marketing clout.

Still, we know that these advantages frequently don't show up on the bottom line. The biggest companies are the most profitable—on the basis of return on equity—in only four out of 67 in the *BUSINESS WEEK* Top 1000.

The most successful big companies are ones that have figured out how to manage themselves as a series of small companies. They usually share certain traits. They push decision-making down to managers who are close to the business. They provide flexibility to move quickly and take financial risk when opportunities present themselves. They focus on businesses where they have a technological or marketing edge.

Johnson & Johnson is a good example. It has a strong record in developing successful new products and in making lots of money, yet it is managed as a collection of 166 autonomous companies. Such successful big companies as Hewlett-Packard, 3M, and Emerson Electric have a similar operating style.

Big companies often get into trouble when they emphasize increased size rather than more basic objectives. General Motors, Navistar, Sears, and Bank of America are all companies that lost their competitive edge when they were preoccupied with bigness.

Corporate managements bent on increasing competitive effectiveness need to look inside their own fences, not at the grass on the other side. And the word in the boardroom should be: Bigger doesn't necessarily mean better.

WHAT'S WRONG WITH WRIGHT

Step back from the House Ethics Committee's investigation of Speaker Jim Wright of Texas for a moment, and weigh the evidence in terms of Wright's fitness as a national spokesman and No. 2 in line of succession for the Presidency. You don't need the judgment of a dozen squirming lawmakers on the ethics panel to conclude that, when it comes to his personal conduct in office, Wright has an ethical blind spot as big as his home state.

Look at the evidence. Twice in 1979, Wright lobbied U.S. and Egyptian officials on behalf of two oil companies that

later offered Wright lucrative investments in gas wells. Wright says he was just looking out for constituents. In 1986, Wright personally intervened with the Federal Home Loan Bank Board on behalf of fellow Texans who just happened to be major Democratic fund-raisers presiding over failing savings and loan associations. Wright insists that he was just looking out for his constituents. His memoirs, printed by the same company that printed his campaign literature, provided him with royalties of 55% for copies peddled to lobbyists and political supporters. Wright says he was all on the up-and-up—and besides, the printer was a personal friend.

A friend in Wright's Fort Worth home district, developer George Mallick, provided Wright with a rent-free apartment for years, plus a Cadillac for Wright's wife. Wright says the arrangements were not improper because Mallick had no legislative interest.

There is a disturbing pattern here. In his decade of leadership, Wright's ego and unswerving loyalty to those he considers his friends have pushed him into arrangements that may not be illegal but show terrible judgment and disregard for the public interest. He's the wrong man for Speaker. He should step aside.

A RAY OF HOPE IN CUTTING THIRD WORLD DEBT

The "Brady plan" for reducing Third World debt is only a sketch so far. But it is a welcome step toward recognizing two realities: the urgent need to ease debt payments to head off political and economic disasters in developing countries, and the crucial role that Japan must play in shoring up the international financial system.

Treasury Secretary Nicholas F. Brady understands that debtor countries won't be able to attract new investment and resume economic growth until their debt loads are visibly diminished by write-downs. That approach contrasts sharply with the philosophy of his predecessor, James A. Baker, who mistakenly believed that the debt problem could be solved simply by urging banks to lend more money to the Third World. Under the Brady plan, Japan would put several billion dollars a year to help Third World nations pay back debts from creditors at discounted prices. This is exactly what Japan itself had proposed, and is welcome proof of Japan's newfound willingness to assume greater responsibility for the economic health and political stability of others.

The U.S. and Europe, of course, must continue to do their part. The Brady plan calls on the International Monetary Fund and the World Bank to provide incentives for voluntary participation by banks in debt write-downs and steps to lower interest costs and stretch out repayment terms for debtors. Financing these incentives eventually will cost U.S. taxpayers money, since the U.S. is the biggest contributor to these institutions. That means the Administration and Congress will need the courage to explain a simple truth: It will cost less to tackle the debt problem now than to let it fester, at the risk of plunging debtors and creditors into a far deeper crisis.

BusinessWeek

APRIL 3, 1989

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Can
Bart
Giamatti
resolve the
growing tensions
over baseball's
new riches?

PAGE 84



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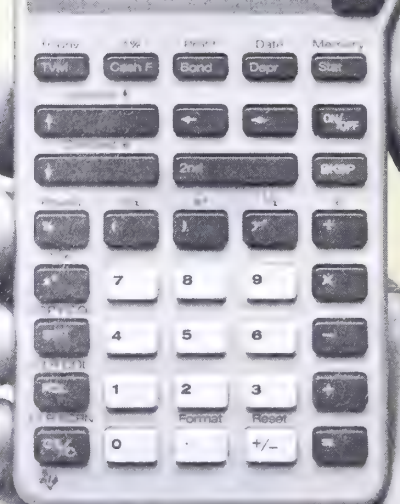
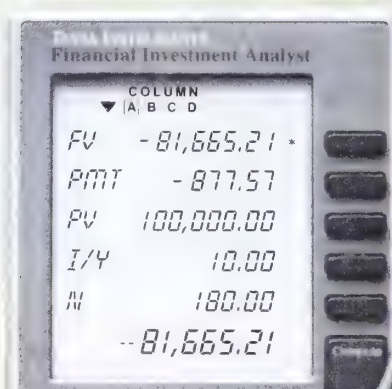
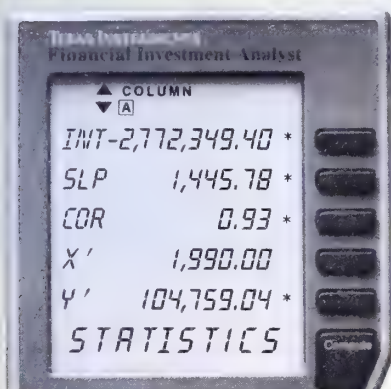
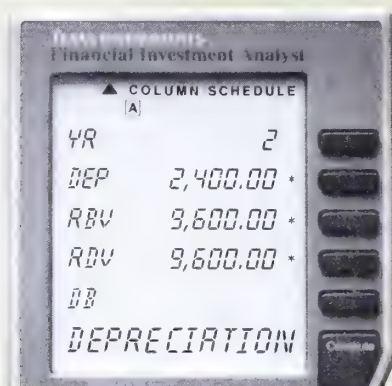
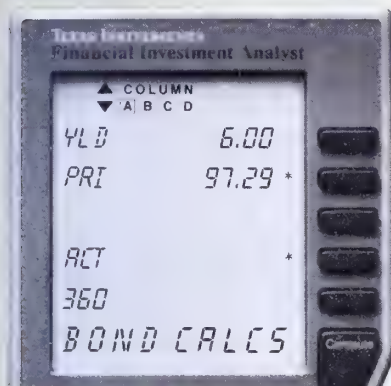
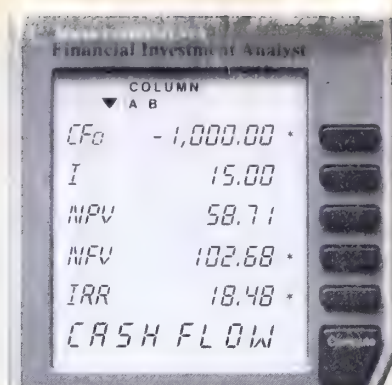
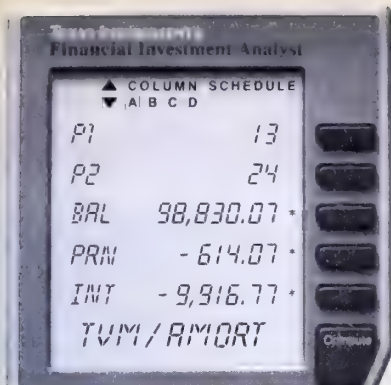
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INSTRUMENTS**



ARTFUL DODGER: FREE AGENCY HAS SENT THE SALARIES OF SUCH SUPERSTARS AS LOS ANGELES' KIRK GIBSON INTO THE STRATOSPHERE

Cover Story

84 PROFESSOR HARDBALL

Bart Giamatti becomes Major League Baseball's seventh commissioner at what looks like a golden moment: The sport is out of its early-1980s slump, drawing record gates and profits. But the infighting among players, owners, and agents has never been fiercer, and Giamatti will have to work fast to avert a 1990 strike. Can he do it? The Yalie already has shown that he can jawbone with the best of them

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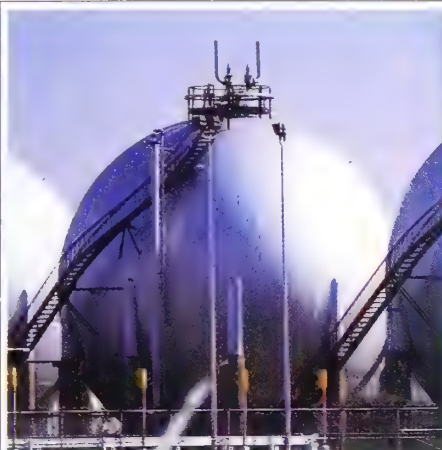
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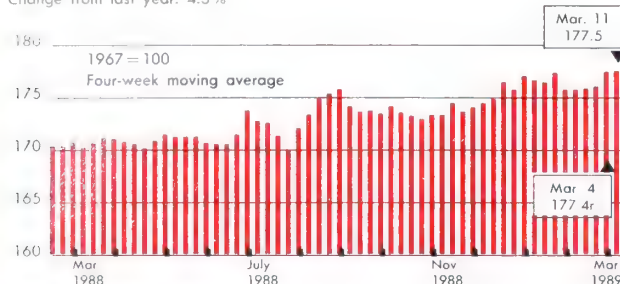
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BusinessWeek Index

PRODUCTION

Change from last week: 0.1%
Change from last year: 4.3%

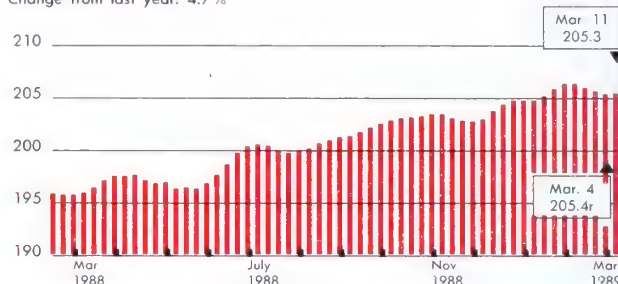


The production index ticked up in the week ended Mar. 11. Since the beginning of 1989, growth in the index has basically been flat. On a seasonally adjusted basis, output of lumber, electric power, crude-oil refining, and steel increased. This was offset by declines in coal, trucks, paperboard, rail-freight traffic, autos, and paper production. Prior to calculation of the four-week moving average, the index dropped to 177.8, from 178.2 in the previous week.

BW production index copyright 1989 by McGraw Hill Inc.

LEADING

Change from last week: 0.0%
Change from last year: 4.7%



The leading index increased slightly for the week ended Mar. 11. Higher stock prices, lower bond yields, and faster growth in M2 and materials prices offset the negative economic signal given by a sharp drop in the growth rate for real estate loans. Data on large business failures were unavailable for the week. Before calculation of the four-week moving average, the index also rose slightly, to 205.5, from 205.1 in the prior week.

Leading index copyright 1989 by Center for International Business Cycle Research

PRODUCTION INDICATORS

	Latest week	Week ago	% Change year ago
STEEL (3/18) thous. of net tons	2,057	2,012 #	3.5
AUTOS (3/18) units	151,409	156,692r #	3.0
TRUCKS (3/18) units	93,743	90,436r #	11.9
ELECTRIC POWER (3/18) millions of kilowatt-hours	51,187	55,640 #	-1.4
CRUDE-OIL REFINING (3/18) thous. of bbl./day	12,490	12,791 #	-4.3
COAL (3/11) thous. of net tons	18,634 #	19,793	3.6
PAPERBOARD (3/11) thous. of tons	731.1 #	748.9r	-2.8
PAPER (3/11) thous. of tons	757.0 #	765.0r	-0.1
LUMBER (3/11) millions of ft.	481.3 #	466.3	-8.6
RAIL FREIGHT (3/11) billions of ton-miles	18.9 #	19.8	0.5

Sources: American Iron & Steel Inst., Ward's Automotive Reports, Edison Electric Inst., American Petroleum Inst., Energy Dept., American Paper Inst., WWPA¹, SFPA², Association of American Railroads.

FOREIGN EXCHANGE

	Latest week	Week ago	Year ago
JAPANESE YEN (3/22)	131	131	127
GERMAN MARK (3/22)	1.87	1.87	1.69
BRITISH POUND (3/22)	1.72	1.72	1.84
FRENCH FRANC (3/22)	6.33	6.34	5.75
CANADIAN DOLLAR (3/22)	1.19	1.20	1.25
SWISS FRANC (3/22)	1.62	1.61	1.40
MEXICAN PESO (3/22) ³	2,381	2,371	2,300

Sources: Major New York banks. Currencies expressed in units per U. S. dollar, except for British pound expressed in dollars.

PRICES

	Latest week	Week ago	% Change year ago
GOLD (3/22) \$/troy oz.	393.350	392.900	-12.5
STEEL SCRAP (3/21) # 1 heavy, \$/ton	115.50	115.50	-2.9
FOODSTUFFS (3/20) index, 1967=100	231.7	231.2	7.4
COPPER (3/18) c/lb.	148.1	153.9	35.6
ALUMINUM (3/18) c/lb.	94.0	101.0	-13.4
WHEAT (3/18) # 2 hard, \$/bu.	4.59	4.51	51.0
COTTON (3/18) strict low middling 1-1/16 in., c/lb.	57.49	56.68	-6.0

Sources: London Wed. final setting, Chicago mkt., Commodity Research Bureau, Metals Week, Kansas City mkt., Memphis mkt.

LEADING INDICATORS

	Latest week	Week ago	% Change year ago
STOCK PRICES (3/17) S&P 500	295.85	293.91	10.
CORPORATE BOND YIELD, Aaa (3/17)	9.79%	9.73%	4.
INDUSTRIAL MATERIALS PRICES (3/17)	104.3	104.3	6.
BUSINESS FAILURES (3/10)	NA	NA	NA
REAL ESTATE LOANS (3/8) billions	\$313.1	\$313.0	12.
MONEY SUPPLY, M2 (3/6) billions	\$3,089.0	\$3,082.4r	4.
INITIAL CLAIMS, UNEMPLOYMENT (3/4) thous.	319	295	1.

Sources: Standard & Poor's, Moody's, Journal of Commerce (index: 1980=100), Dun & Bradstreet (failures of large companies), Federal Reserve Board, Labor Dept. CIBCR seasonally adjusts data on business failures and real estate loans.

MONTHLY ECONOMIC INDICATORS

	Latest month	Month ago	% Change year ago
HOUSING STARTS (Feb.) annual rate, thous.	1,498	1,690r	-0.9
INDUSTRIAL PRODUCTION (Feb.) total index	141.1	141.1	5.0
PRODUCER PRICE INDEX (Feb.) finished goods	112.1	111.0	5.
CONSUMER PRICE INDEX (Feb.)	121.6	121.1	4.8

Sources: Commerce Dept., Federal Reserve, BLS

MONETARY INDICATORS

	Latest week	Week ago	% Change year ago
MONEY SUPPLY, M1 (3/6)	\$791.5	\$788.8r	4.
BANKS' BUSINESS LOANS (3/8)	311.2	312.0r	5.
FREE RESERVES (3/8)	362r	656r	-47.
NONFINANCIAL COMMERCIAL PAPER (3/8)	110.8	110.3	26.8

Sources: Federal Reserve Board (in billions, except for free reserves, which are expressed for a two-week period in millions).

MONEY MARKET RATES

	Latest week	Week ago	Year ago
FEDERAL FUNDS (3/21)	9.80%	9.78%	6.51%
PRIME (3/22)	11.50	11.50	8.50
COMMERCIAL PAPER 3-MONTH (3/22)	10.10	9.87	6.62
CERTIFICATES OF DEPOSIT 3-MONTH (3/22)	10.25	10.00	6.62
EURODOLLAR 3-MONTH (3/15)	10.10	10.03	6.73

Sources: Federal Reserve Board, First Boston

Row data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment
1= Western Wood Products Assn. 2= Southern Forest Products Assn. 3= Free market value NA= Not available r= revised NM= Not meaningful



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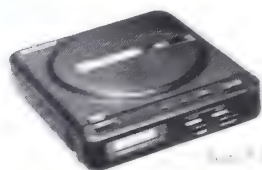
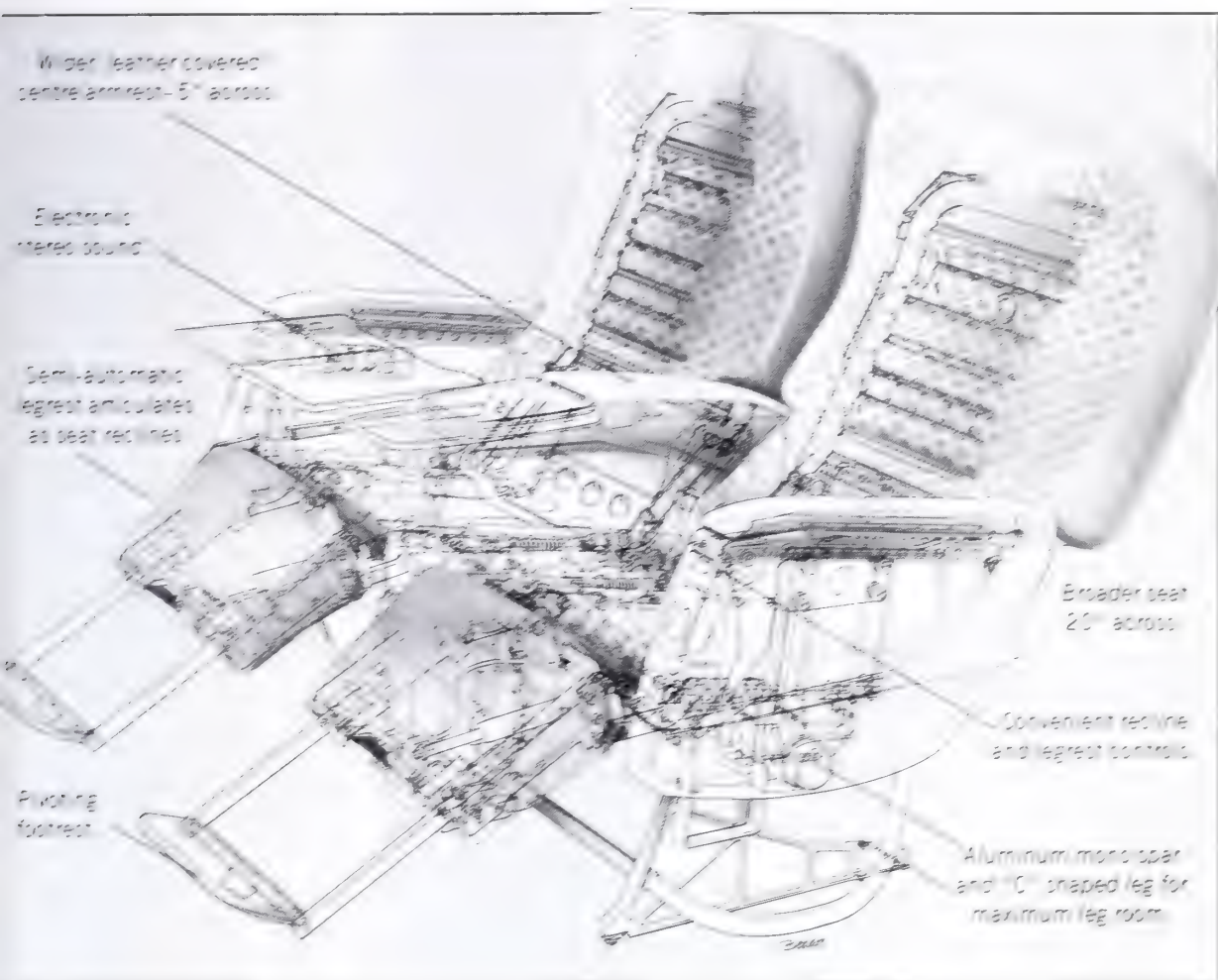
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CORPORATE TAXES: THE U.S. IS SHOOTING ITSELF IN THE FOOT

A better remedy than protectionism" (Editorials, Feb. 27) hits the mark in its keen recognition of the necessary interdependence between U.S. tax and trade policy. For our long-term competitive standing, we must acknowledge the need to join the two by enacting a consumption-based tax, such as a value-added tax, while simultaneously reducing—or ultimately eliminating—corporate income taxes. A consumption tax that incorporates the notion of border tax adjustments (i.e. rebating the tax on exports) would make U.S. exports more attractive in foreign markets, while raising corporate income taxes would have just the opposite effect. Furthermore, with the Japanese Diet's recent passage of a 3% value-added tax, and Canada now laying the appropriate groundwork for such a tax, the U.S. will be left as the only major industrial nation depending mainly on the income tax.

In the face of our enormous trade and budget deficits, both President Bush and we in Congress have a responsibility to recognize—and act upon—the undeniable interdependence between domestic tax policy and our competitive standing in an unforgiving global economy.

Representative Dick Schulze (R-Pa.)
 U.S. Congress
 House Trade Subcommittee
 Washington

WOULD DAN QUAYLE RECOGNIZE A SKILLED LABORER IF HE SAW HER?

In "Introducing Dan Quayle, Competitiveness Czar" (Top of the News, Feb. 27), Dan Quayle correlates the high percentage of women, minorities, and immigrants entering the work force with a shortage of skilled labor by the turn of the century. Such a comment blatantly assumes that only white, American-born, male employees constitute skilled labor. As a woman and an immigrant with an engineering PhD, a Harvard MBA, and a decade of work experience in American manufacturing companies, I (and many thousands like me) contribute more every day to the skills and competitiveness

PUBLISHER'S NOTE

In our Mar. 13 article about Bear Stearns, we cited as an example of third-party comments on Bear Stearns' reputation a report that Bear Stearns had "hiked its fees" to Triton Group Ltd., for whom Bear Stearns handled a private placement.

As stated in our Correction in the Mar. 27 issue, we have now verified that, in fact, Bear Stearns lowered its fees. We wish to apologize for any disparagement of Bear Stearns' business ethics that this factual misstatement has caused.

John W. Patten

John W. Patten, Publisher

of the U.S. work force than any White House task force is likely to do.

Mary P. Quin
 Rochester, N. Y.

CIVIL SERVANTS CAN'T SERVE WITHOUT DECENT PAY

As an Internal Revenue Service manager in the trenches, I disagree with Gary Becker's assertion that government jobs already pay more than comparable private employment ("Federal pay: Only top-to-bottom reform will do," Economic Viewpoint, Feb. 13). In the last two years the IRS North Atlantic Region (New York and New England) lost 11,600 employees through resignations, retirements, and firings. Attrition rates for the entire IRS range from 16% for special agents to 57% for data transcribers. The number of applicants is 24% lower this year than last year. And last year was 50% lower than 1987.

If Professor Becker is right, why did some IRS facilities stop administering the civil-service tests to facilitate hiring? Why are our starting salaries less than what unskilled factory help is paid? Is he satisfied with the quality of our employees when we answer only 3 out of 4 tax questions correctly? Can he explain why lawyers and accountants are complaining about the lack of knowledge

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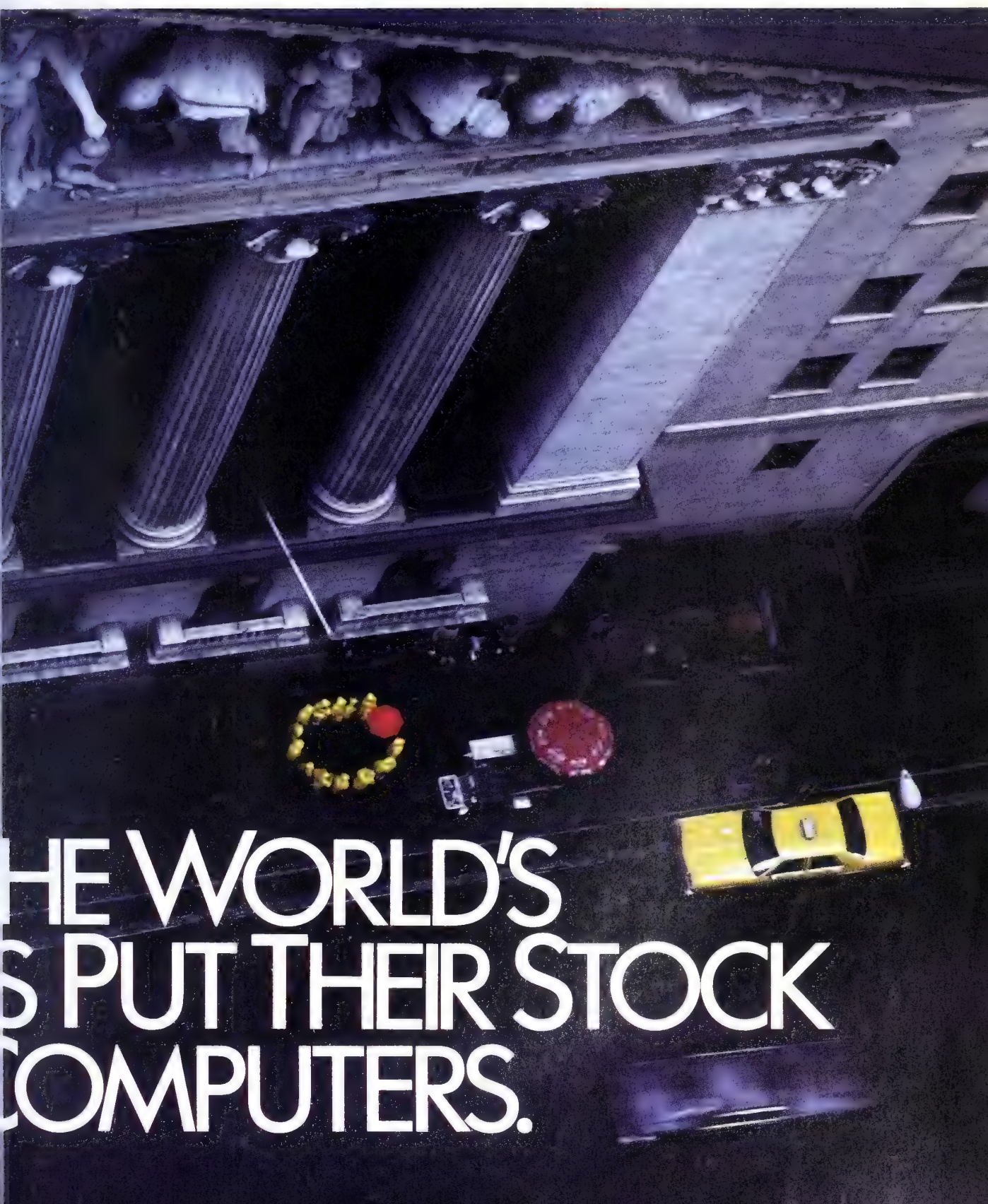


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An aerial, high-angle photograph of a classical building with prominent columns and a pediment. Below the building, a street scene is visible with a yellow taxi, a red car, and a yellow flower arrangement. The text "THE WORLD'S PUT THEIR STOCK COMPUTERS." is overlaid in large, white, sans-serif capital letters at the bottom left.

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Readers Report

and competence of IRS agents, auditors, and attorneys? All of these problems are the result of federal employees being substantially underpaid.

Frederick Cohen
Chief, Processing Div.
IRS Center
Holtsville, N. Y.

The question of whether to give Congress its pay raise has created a re-ounding conflict, but one that I believe can be resolved easily. Give congressmen and women their raise. They need it. And if they don't get it, they will serve us even more poorly than they have in the past. But I would like to make the following suggestion: Index their pay to inflation. Easy now. You're going to say that Congress causes inflation by their irresponsible spending, right? Fair enough. Here's the index: annually, for every percent that inflation goes up, Congress gets the same percentage cut from their pay.

Folks, we would get to see a religious experience from D. C. that you gave up paying for years ago.

Sunny King
Mesa, Ariz.

MONSANTO: ONE QUARTER DOES NOT A DISASTER MAKE

Reports of our sickly status to the contrary ("Corporate profits: The old expansion is paying new dividends," *Top of the News*, Feb. 13), Monsanto is alive and well—and quite healthy, thank you. With net income in 1988 up 36%, earnings per share up 47%, and return on equity up to 15.6% from 11%, Monsanto celebrated its best year ever.

If you only focus on fourth-quarter results, you won't get a true picture of any company's financial performance. Monsanto's fourth quarter is traditional—light—the purchasing patterns of our major customers makes that inevitable. There are enough pressures on companies to think quarter-to-quarter, sacrificing long-term growth for short-term gain. It would help if major business publications did not add to it.

Mark Schannon
Public Relations Director
Monsanto Co.
St. Louis

WHY WORKERS WANT TO GET OFF THE TEAM

John Hoerr charges us with saying that work teams are no good for workers "anytime or anywhere." ("Is teamwork a management plot? Mostly not," *Labor*, Feb. 20). In fact, in our book, *Choosing Sides: Unions and the*

NORTHWEST

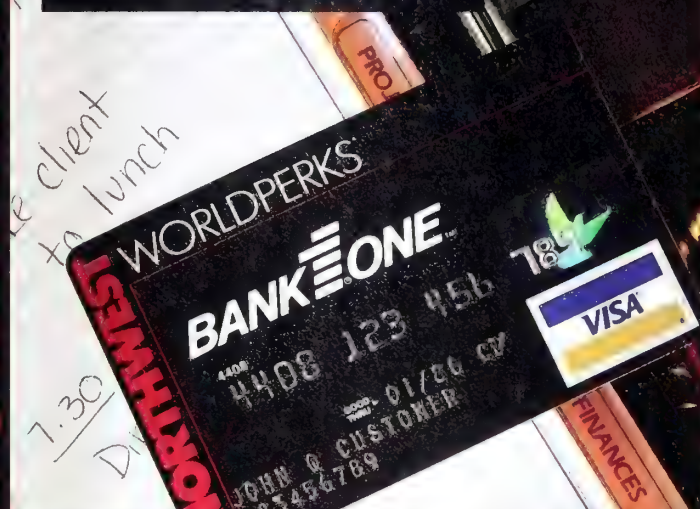
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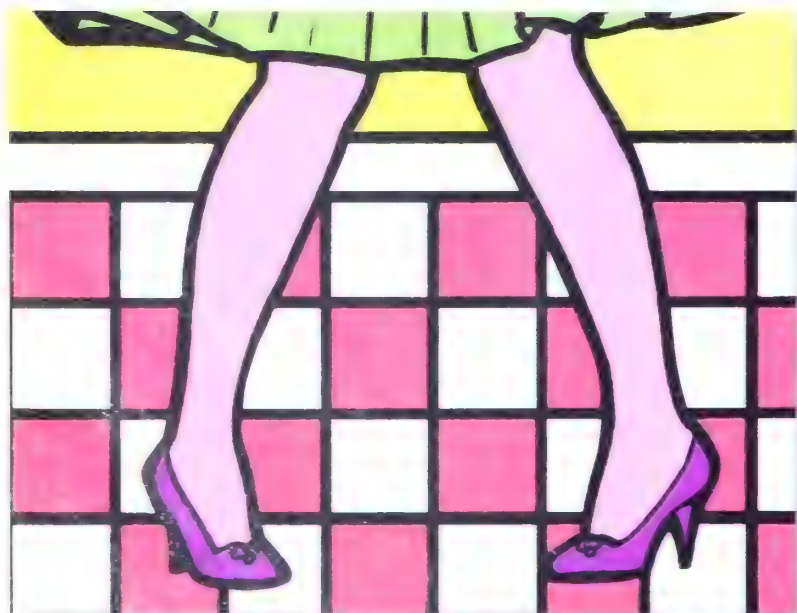
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Readers Report

Team Concept, we argue the opposite: that it would be quite possible for a team type of work organization to provide both a quality product and more rewarding jobs.

Unfortunately, management in the auto industry is pushing a different type of team concept, which we call "management by stress," modeled after such plants as NUMMI and Mazda. Workers here say that rather than teamwork, working conditions are an intense version of Hoerr's description of a traditional plant: "employees confined to a narrow set of minutely described tasks and watched over closely by a supervisor." With management having the strong upper hand, and with many union leaders accepting management's arguments, workers have had little luck in establishing a more collegial form of teamwork. Yes, as Hoerr says, it is the union's job to prevent speedup. That's why there is a New Directions rebellion within the UAW. These unionists are demanding that their leaders get off management's back and onto the rank and file's.

Mike Parker
Jane Slaughter
Labor Notes
Detroit

SOMETIMES A COMPANY'S SURVIVAL IS SPELLED LBO

As an investment banker whose firm has arranged financing for nearly 10 leveraged buyouts of companies over the past five years, I would like to comment on "Why Washington may not lay a glove on LBOs" (Finance, Feb. 6).

Any cure for the excessive use of LBOs may be worse than the disease if it impairs the ability of entrepreneurs to buy and sell privately held companies. Each year a number of these companies pass from one owner to the next, thanks to LBO financing. Generally, there are either superfluous operations that can be sold to pay down debt nor a legion of unnecessary employees that can be dis-

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Readers Report

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Russell Hindin
Managing Director
Hindin/Owen/Engelke Inc.
Los Angeles

GOING BANKRUPT IS NOTHING TO BE PROUD OF

Let me get this straight: Global Marine's management bet the ranch, bit the bullet (Chapter 11), emerges "nearly scathed," and few hold management responsible ("Now all Global Marine needs is a market," Top of the News, Mar. 13)? Your writer is too kind! I have never seen a firm with a top-grade board that had to declare bankruptcy.

There are many examples of drilling contractors, both land and offshore, that did not bet the ranch, did not declare bankruptcy, and are still paying interest on their debt. These well-managed companies have had to compete with other contractors that have opted for Chapter 11 and have been able to price their services without the necessity to pay interest and principal on their debt.

I have worked with firms in restructuring and never found it necessary to resort to bankruptcy. In many cases it results from poor management and creditors' low expectations of management. Chapter 11 should go hand-in-hand with the replacement of top management.

R. L. Hassell
Hassell & Associates
Dallas

CORRECTION

In the Mutual Fund Scoreboard (Feb. 1988), the 1988 total return for FPA Paramount Fund was wrong. The correct figure is 19.8%. Also, Rushmore Stock Market Plus Fund is a no-load fund. It does not have a 2% deferred sales charge.

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DESTRUCTIVE GENERATION: SECOND THOUGHTS ABOUT THE '60s

By Peter Collier and David Horowitz
Summit • 352pp • \$19.95

THIS IS THE DAMNING OF THE AGE OF AQUARIUS

The Sixties. They haunt us still. To be young then, free from restraints and battling an evil "system" was to live a life of eternal promise. Viewed as extending from the election of John F. Kennedy in 1960 to the withdrawal of U.S. troops from Saigon in 1973, the Sixties were a "long decade" full of social change and personal liberation for millions.

Now those who admonished: "Don't trust anyone over 30" are over 40. Anti-Establishment then, they are authority personified now—parents, managers, property owners. The children of the Sixties, finally slipping into these grown-up roles, are still confronting questions about values and institutions. But their answers are different from those of 20 years ago. Talking about education, drugs, sex, work, money, and property,

they are beginning to sound a lot like—uh-oh—the parents, teachers, even politicians they rebelled against. The public schools are decaying, they say, the drug scene is deadly, and politics belongs to the special interests.

What's especially strange for the Sixties set is a nagging self-doubt. Self-righteousness to the point of sanctimony was the generation's hallmark. Now many wonder if they have some responsibility for the current social morass. In their idealistic fight against the war, racial discrimination, and other social problems, did they do harm as well as good?

Destructive Generation: Second Thoughts About the '60s shouts an emphatic "Yes!" The book, by Peter Collier and David Horowitz, is the most strident example of a growing neoconservative backlash against the period. While many

aging "Movement" leaders, such as Tom Hayden, have celebrated the era in print with fond nostalgia, Collier and Horowitz look back with a colder eye.

In a loose collection of chapters on the Black Panthers, the Weather Underground, and the New Left, the authors go inside radical organizations, depicting the key personalities and debates of the volatile era. All the examples are used to convey a single theme: The white, middle-class radical leaders were naive, foolish romanticists who were duped by tougher, more "streetwise" heroes whether Huey Newton or Ho Chi Minh.

The book's strength is its details. They range from the sexual manipulateness of Weatherwoman Bernadine Dohrn to the intended destination of the bomb that exploded in a Greenwich Village townhouse in 1970, killing three radicals. The target: a Fort Dix dance hall full of young recruits and their dates.

The heart of the book, however, is a cry of betrayal by the authors, who were "Movement heavies" themselves—editors of the New Left *Ramparts*—before writing such best-selling family biographies as *The Rockefellers* and *The Kennedys*. The last two chapters, the book's best, are first-person accounts



each author's odyssey from radical to conservative. In the end, the sense of betrayal is critical. Who betrayed the generation? Their heroes, naturally. For middle-class academics, as Collier and Horowitz see it, the great Congress were the most "righteous" heroes, indigenous revolutionaries fighting the imperialists for freedom. But the aftermath of the war shattered the radical

vision. As Communists from North Vietnam dominated the South, the myth of Viet Cong heroism evaporated. Worse, the million and a half boat people, the "reeducation" camps, and the anti-Chinese pogroms showed the Communist regime to be worse than any U.S.-backed Vietnamese dictatorship. While much of *Destructive Generation* has the ring of truth, the disillusioned children of the Sixties deserve better. Presented as "an honest inventory of our generation's impact," the book exudes self-loathing and contempt



so intense and one-sided that it caricatures the era's anti-Establishment rhetoric. "The Movement had long since destroyed itself through sectarian ecstasies and cannibalism," the authors write, "with each new year bringing a few pathetic Weathermen in from the cold after unglamorous underground lives waiting tables and watching afternoon soap operas." It's as if Collier and Horowitz, feeling betrayed, rebottled their fury and turned it inward.

There is much to the authors' central argument that by attacking all author-

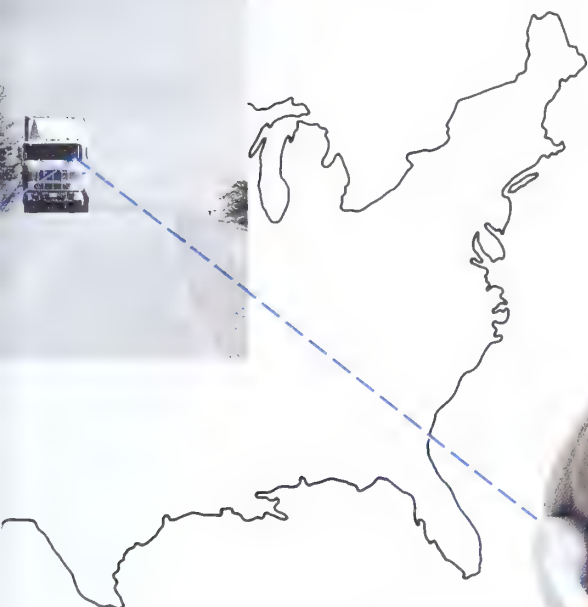
ity, the young leftists of the Sixties destroyed the American consensus of values and the institutions based on them. Everything became relative. In education, for example, calculus is not to be valued more than basketweaving, and "life experience"—credit for living—may be seen as the equivalent of a degree in history. Values, Collier and Horowitz write, have

been rendered confusing and virtually meaningless.

Unfortunately, the authors' furious rhetoric obscures the retrospective insights they claim for themselves. The Sixties generation never did create their Revolution, but they did, after all, make revolutionary changes. It will fall to others to offer a wiser assessment of their accomplishments and failures.

BY BRUCE NUSSBAUM

Senior Writer Nussbaum went through college, the Peace Corps, and grad school during the "long decade."



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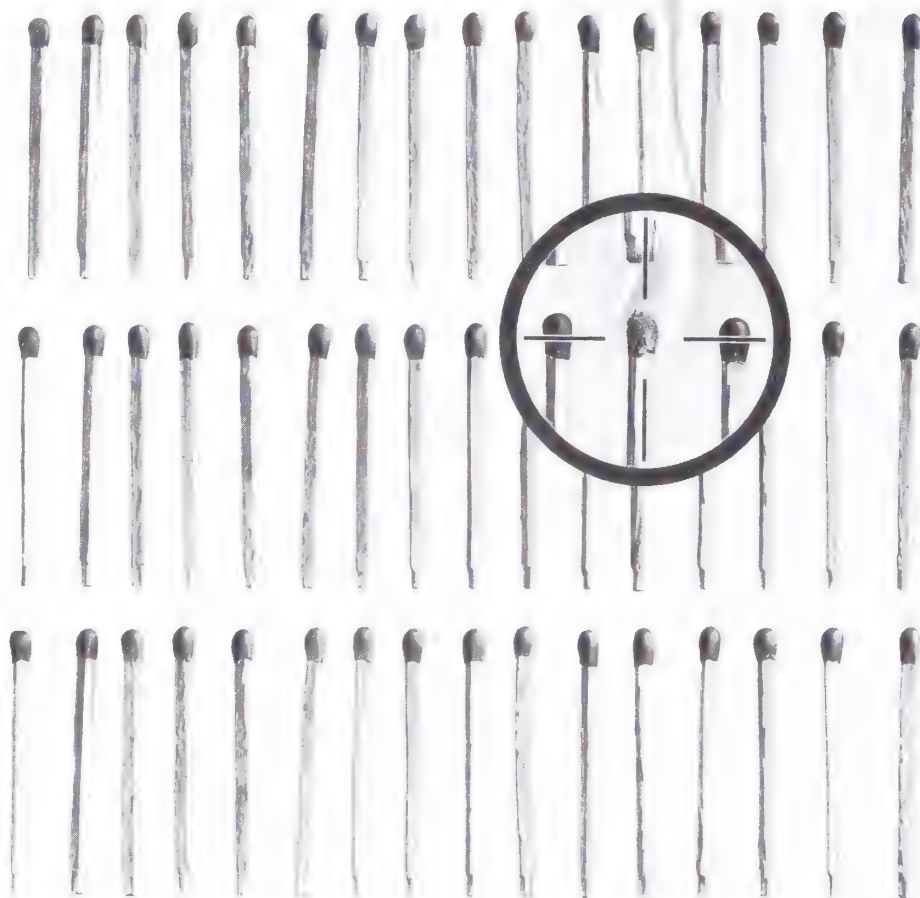


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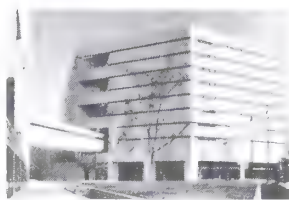


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DITCH THE CAPITAL-GAINS TAX ONCE AND FOR ALL

BY PAUL CRAIG ROBERTS



As things stand now, investment income is often subjected to corporate, personal, and capital-gains taxes. That hurts the economy as much as it hurts taxpayers

If the U.S. Tax Code were a person, it would go to hell for its covetousness. The code's architects certainly ignored the 10th Commandment when they designed a tax system that punishes the successful regardless of the economic consequences.

In pandering to envy, our tax laws reduce the accumulation of capital by subjecting investment income to multiple taxation. Consequently, the rate of return that an individual earns from an investment is substantially smaller than the value of his investment to society, as measured by such factors as improved labor productivity and higher wages. Thus, taxation causes investment to fall far short of the levels that are socially desirable.

Consider the extraordinary tax bias against saving and investment: The amount of money a person has to save and invest is first reduced by the personal income tax. If his or her aftertax savings are invested in a corporation and used to purchase capital equipment, the income earned by the investment is taxed at the corporate rate and then again at the personal rate if paid out in dividends.

If the income remaining after corporate taxes is instead retained and reinvested, the expected earnings will be reflected in the market value of the stock, adjusted for future corporate taxation. If the owner sells the stock and realizes a "capital gain," then this amount is subject to further taxation. These multiple layers of taxation are further compounded by the property tax, resulting in reduced investment and lower growth in labor productivity.

CONFISCATION? Not content with enshrining envy in our tax code, its architects have perpetuated fraud by including a capital-gains tax in the income tax—even though the national income accounts don't regard capital gains as income or include them in the measurement of gross national product. A capital-gains tax is a wealth tax. It taxes the rise in the price of an asset, reflecting either inflation or the stock market's estimate that a company's future earnings will be higher.

If the price of the asset rises because of inflation, there is no real gain at all, and the tax is nothing but a confiscation device. On the other hand, if the price rises because the company's earnings improve, these earnings will be doubly taxed as corporate and dividend income. Taxing the capital gain bites into the same income a third time.

When the unfair capital-gains tax hurts investment in people's homes, we provide a special exclusion. But when it hurts investment in plant and equip-

ment, envy crowds out logic, and the economy suffers.

Capital gains are taxed because it is widely, but mistakenly, believed that they go primarily to "the rich" who already have "too much." The Ten Commandments reflect far more knowledge about the deleterious economic consequences of envy than our policymakers; they also show a better command of the facts.

Internal Revenue Service data show that the roughly 3 million taxpayers with recurring annual incomes below \$20,000 receive a larger share of total capital gains than taxpayers earning more than \$200,000. Moreover, 50% of all capital gains go to people earning less than \$60,000. The average capital gain of lower-income people who report those gains is far too small to support the common but fallacious argument that they're really rich people hiding behind tax shelters and municipal bond income.

Who are these poor and middle-class people receiving capital gains? They're widows and retired people living off savings or children being educated with the proceeds of a dead parent's estate.

EBB AND FLOW. The erroneous claim that the rich are the primary beneficiaries of capital gains is based on a dishonest definition of rich that includes onetime capital gains that reflect a lifetime of work. For example, a middle-class businessman retires and sells his business. That year the capital gain swells his income to several hundred thousand dollars, and he is "rich" for the year. The next year his income goes back down to middle-class levels, and someone else sells a business, becoming rich for a year.

The imbecilic argument that untaxed capital gains are a windfall for the rich and subtract from the funds available to "help people" has no basis in theory or fact. Eliminating the capital-gains tax would reduce the cost of capital and increase investment, which in turn raises labor's productivity and income.

The capital-gains tax also slows the formation of new capital. The only people helped by the tax are those with old, established wealth. New capital unleashes upstarts who bust up the status quo, create opportunities, and undermine the protected enclaves of the rentier class, including many large corporations. New capital is the best thing an egalitarian society has going for it.

Recognizing this, President George Bush proposed a reduction in the capital-gains tax rate. Critics, however, are up in arms: It would let the rich benefit along with the rest of us, so let's cut off our nose to spite our face. Ignorance and envy drive U.S. tax policy, and ideologues intend to keep it that way. ■

PAUL CRAIG ROBERTS HOLDS THE WILLIAM E. SIMON CHAIR OF POLITICAL ECONOMY AT THE CENTER FOR STRATEGIC & INTERNATIONAL STUDIES IN WASHINGTON

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EDITED BY GENE KORETZ

HIGHER OIL PRICES ARE CASTING AN OMINOUS SHADOW

With the oil market continuing to show surprising strength, a number of economists have begun to factor the recent price runup—some \$4 to \$5 a barrel since mid-November—into their economic projections. To put it mildly, they do not like what they see.

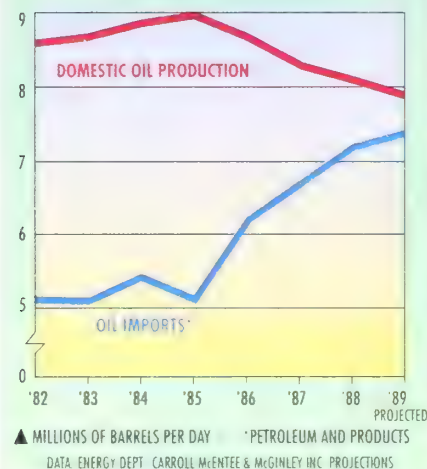
Concern is high because oil often plays a dramatic role in trade and inflation developments. Shifting oil prices, for example, have caused the U.S. oil import bill in the 1980s to fluctuate from

been falling since the 1986 oil price collapse, he notes, and it is likely to come in at less than 8 million barrels per day this year—the lowest level in at least 16 years. Meanwhile, growing U.S. oil demand, which accounts for some 30% of world consumption, has been sucking in a rising tide of imports (chart).

Even with rising prices, Hunt predicts that it will take years for U.S. oil production to begin to expand again. He points out that the active domestic rig count fell to a new all-time low in February, and that it normally takes three to five years before a significant pickup in rig activity begins to affect output.

Meanwhile, the oil import surge is retarding progress in reducing the trade imbalance. Michael Evans of Evans Economics calculates that an average price of \$18 for imported oil this year could raise the nation's oil import bill by some \$12 billion. And the outlook in the years ahead is no less troubling, concludes a recent study by Harold T. Gross and Bernard L. Weinstein of Southern Methodist University's Center for Enterprising. Assuming oil prices range from \$14 to \$28 per barrel, they estimate that the oil import bill will rise to between \$70 billion and \$83 billion annually by 1995.

OIL IMPORTS SURGE AS OUTPUT FALLS



a high of nearly \$80 billion early in the decade to a low of \$35 billion in 1986. Last year oil imports ran about \$39 billion, roughly a third of the trade deficit.

Similarly, soaring oil prices helped fuel the double-digit pace of consumer inflation at the start of the decade, while the subsequent price decline was largely responsible for the drop in inflation to below 2% in 1986. As recently as last year, estimates economist Lacy H. Hunt of Carroll McEntee & McGinley Inc., declining oil prices lowered the reported consumer inflation rate by one percentage point. And if current prices hold, they could well have the opposite effect this year (page 32).

To be sure, many experts still believe that prices will weaken later this year as U.S. economic growth slows and OPEC discipline inevitably wanes. But Hunt predicts that increasing U.S. dependence on world oil supplies will keep prices on an upward course for the next three or four years. U.S. oil output has

THE BUYOUT BINGE IS SLASHING SAVINGS...

Don't blame the shortfall in national savings on government profligacy, warns a new American Business Conference study written by George N. Hatsoopoulos, chairman of the Boston Federal Reserve Bank, and economists Paul R. Krugman and James M. Poterba of Massachusetts Institute of Technology. While conceding that growth of the federal deficit has reduced national savings—which is the sum of private and government savings—the authors contend that declining private savings has been the chief culprit.

Statistics tell the story. From an average 7.9% of national income in the 1970s, savings declined to just 2.1% in the period from 1985 through 1987. The reason: a slight rise in total state, local, and federal government spending, from 22.8% of national income in the 1970s to 23.8% in the 1985-87 period, and a much larger jump in private consumption from 69.3% to 74.1%.

The study's most intriguing finding concerns the ways in which "overconsumption" by individuals has been fostered by the boom in debt-financed acquisitions and leveraged buyouts. Corporations shifting from equity- to

debt-financing generally pay out more interest than in dividends, the study notes, thus providing households with higher interest receipts that are available for consumption.

More important, by forcibly converting equities into cash, LBOs and takeovers virtually thrust the money into the hands of investors. Economists have generally assumed that most of the cash was reinvested by its predominantly wealthy recipients. But the authors found that investors have been spending an astonishing 50% of the profits received from buyouts and takeovers, compared with just 3% of their paper gains.

With Paul Magnusson in Washington

... AND LIMITING LBOs COULD GIVE EXPORTERS A BOOST

The Bush Administration's proposal to slow the pace of leveraged buyout by allowing partial deductibility of dividends in exchange for limiting the deductibility of interest could also provide some help on the trade front, contend economist Burton Zwick of Kidder, Peabody & Co. His analysis indicates that the "winners" in such a scheme—industries that pay high dividends relative to interest charges—would include computers, chemicals, electrical machinery, and motor vehicles, while the highly leveraged losers would include retailing, primary metals, textiles, and services.

"As it happens, the winners in this tabulation tend to be far more trade sensitive than the losers," says Zwick. "Thus, rebalancing the tax deductibility of corporate capital might actually enhance the nation's competitiveness."

WHAT'S RAINING ON HOMEBUILDING? NOT THE WEATHER

Shifting weather conditions weren't responsible for the 11.4% drop in housing starts in February, says economist David H. Resler of Nomura Securities International Inc. While he concedes that starts fell from a lofty January level distorted by unusually mild weather, Resler notes that housing permits, which are less sensitive to swings in the weather, posted large declines in both months. Moreover, starts in the West and South, where winter has less effect than in other regions, are down 7.5% since November. "Higher mortgage rates have finally touched off the expected decline in homebuilding," he concludes.

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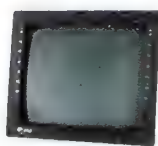
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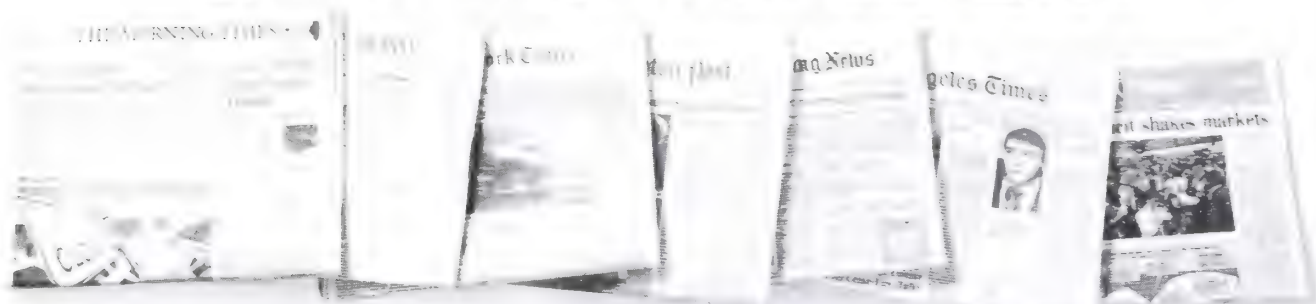
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(All Times Eastern)	6:30	7:00	7:30	8:00
Top Business News	6:30	7:00	7:30	8:00
Financial News	6:35	7:05	7:35	8:05
Small Business News	6:40	7:10	7:40	8:10
Special Business Features	6:50		7:50	
CEO Close-Ups		7:15		8:15
Internat'l Business Line		7:25		



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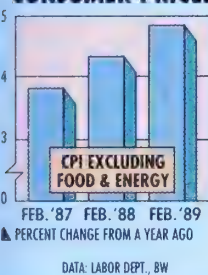
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STEEPER INFLATION MAY BE SETTLING IN FOR A LONG STAY

Accelerating inflation and the Federal Reserve Board's determination to keep it under control will severely test the mettle of this lengthy economic expansion. That classic combination has stopped business upswings cold throughout the postwar period. Investors are increasingly worried—and with good reason—that the Fed will repeat past mistakes by pushing too hard on the brakes.

A BROAD SPEEDUP IN CONSUMER PRICES



The recent market-rattling performance of producer prices, combined with steady upward pressure on consumer prices, is a sign that even more Fed tightening and further hikes in interest rates are on the way. Producer prices jumped 1% in both January and February—a 12.6% annual rate. The consumer price index was up a milder 0.4% in February, but it had risen 0.6% in January—a two-month annual rate of 6.1%. More important, higher inflation is becoming embedded in the economy. The recent speedup has been broad—not confined to the impact of OPEC decisions or the effects of last year's drought. The core rate of consumer price inflation, best measured by the CPI excluding food and energy, has been drifting higher for the past two years (chart). Only recently has this become widely evident (page 32).

CONSUMERS MAY START FEELING THE PINCH

So far the economy has absorbed the Fed's yearlong rise in interest rates with little trouble. Housing sales and construction were both stronger in the second half of last year than in the first half. Car sales were lackluster early this year, but Detroit's latest round of incentives is likely to boost sales in March and April.

Consumer spending in general has been buoyed by strength in the labor markets, robust income growth, and a high level of consumer confidence. Those forces will keep propelling spending through spring and into summer. And consumer demand will be an important prop under industrial output.

But later this year the expansion could face its big hurdle. That's when consumers will most likely start feeling the bite of higher interest rates. Housing may already be showing some strain. Housing starts in February plunged 11.4%, to an annual rate of 1.5 million. That more than wiped out the 7.2% jump in January that was caused by the month's unusually mild weather. And

when Detroit withdraws its incentives, car sales are likely to weaken again.

A worrisome scenario is taking shape: Slower growth in domestic demand threatens to hit at the same time that foreign demand is losing steam. Export growth has already fallen off sharply. That, by itself, has dampened the pace of industrial production since last summer, and factory orders have weakened in early 1989. Taken together, slowdowns in foreign and domestic demand would stall the economy's main engine—manufacturing.

A STRONG DOLLAR DAMPENED EXPORTS

For now industry's vital signs are still good, but they're not as strong as they were last year. Industrial production has slowed in recent months. After growing at an annual rate of 7.1% in the third quarter, output expanded by just 4.6% in the fourth quarter. Growth probably slipped to a 3.5% clip in the first quarter. But that slower pace is still faster than growth in the overall nonfarm economy, and it's a healthy rate for so late in the expansion.

The recent monthly pattern in industrial production shows once again how warm weather in January stole strength from February's data. Output at the nation's factories, utilities, and mines was unchanged in February after rising 0.4% in January. In manufacturing, output was also unchanged after jumping a strong 0.7% in January. Output should rebound in March.

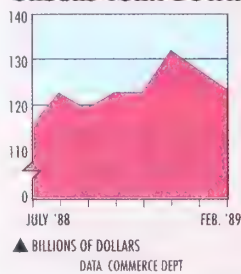
The slower pace of production shows up in the recent weakness in new orders for durable goods. Orders coming in to hardgoods factories fell 3.6% in February, to \$123.7 billion, following a 2.9% drop in January (chart). Bookings have been more volatile than usual lately because of booming aircraft orders combined with the always unpredictable defense sector.

But these were the first back-to-back declines since early 1986, before the export surge began.

The February weakness in orders was also widespread. Defense orders posted a strong rise, but bookings in nonelectrical machinery fell, and orders in both primary metals and transportation equipment were down for the second consecutive month. Electrical machinery showed a small gain.

Still, the trend in durable goods orders remains up. Orders through the first two months of the first quarter

DURABLE GOODS ORDERS TURN DOWN

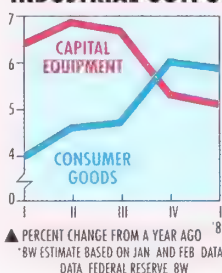


are about even with their fourth-quarter average. That means the outlook for the industrial sector is less troublesome than the January and February weakness in orders appears to imply.

The Fed's tightening over the past year may have relieved some demand pressures on U.S. suppliers—but not from domestic sources. The Fed helped bolster the dollar in 1988 by raising interest rates. And the stronger dollar dampened export demand. That's where industrial output seems to have slowed the most.

This is plain in capital goods, where products are very sensitive to exchange rates. Growth of capital-equipment output has slowed since early 1988, and new orders for nondefense capital goods dropped a sharp 8.9% in February. Weaker defense spending is one reason, but more important, exports of capital goods—one-third of all shipments abroad—have tapered off. In January they stood only 3.1% above year-ago levels. During the previous year these exports rose by more than 41%.

SPLIT TRENDS IN INDUSTRIAL OUTPUT



U.S. production of consumer goods, which is far more dependent on domestic demand, is still growing strongly (chart). It has been accelerating for more than a year now and stands 5.9% above a year ago.

So even with foreign demand moderating, domestic spending is still expanding fast enough to boost output and keep operating rates at levels where price

gains accelerate. That's obvious from the continued speedup in producer prices. The rate of capacity utilization for all industries did slip to 84.3% in February, from 84.5% in January. That coincides with the weather-related distortion in output, but it's still a high rate compared to other expansions.

In general, industries that have been able to make

price increases stick are those that have been running full tilt. But some with high operating rates have been slow to raise prices. The reason: imports.

Producers of textiles and automotive parts, for example, are using about 90% of their capacity. But because both industries have been bombarded by foreign competitors, prices at the producer level for these two products have risen little more than 2% over the past year.

INDUSTRY IS PASSING COSTS ALONG

As raw materials prices keep rising, even these producers may have little choice but to pass along the higher costs. Producer prices of crude materials did fall 0.1% in February, but they're still 6.6% above year-ago levels. Prices of intermediate materials and supplies, up 0.5% in February after a 0.9% advance in January, have accelerated to a 6.3% rate during the past year.

Those rapid paces aren't surprising. Capacity is tightest farther back in the production process. The operating rate for all primary processing stood at 88% in February. That means producers there can continue to raise prices with little concern about business falling off.

The problem is that producers of finished goods may already be passing on those higher costs. The surge in prices of finished goods in January and February was broad and not confined to just food and energy. Food prices rose 1.2% in February, and energy costs were up 2.4%. But even excluding these two volatile items, prices still rose a strong 0.6% in February, with a 0.7% rise in the prices of finished consumer goods.

Some of the producer-price gains in February—such as a 158% increase in the wholesale cost of tomatoes—were aberrations that will be reversed in March. But there can be no denying that inflation's overall pace is quickening. Demand for goods is strong enough that higher prices can now be passed along through the production process to the consumer. So more bad news on consumer prices is probably on the way.

THE WEEK AHEAD

LEADING INDICATORS

Wednesday, Mar. 29, 8:30 a.m.

Most economists expect that the composite index of leading indicators will post a small 0.1% decline in February. Declines in the inflation-adjusted money supply, consumer expectations, and vendor deliveries, along with a rise in initial unemployment claims, will offset higher stock prices and a faster growth rate for sensitive materials prices. The index of coincident indicators—which gauges current economic activity—was likely unchanged in February, after jumping 1% in January. The expected drop in the leading indicators does not by itself imply any serious slowdown. The index increased a strong 0.6% in January and 0.7% in De-

cember. Over the past year it has increased a substantial 5%.

NEW SINGLE-FAMILY HOME SALES

Wednesday, Mar. 29, 10 a.m.

New homes probably sold at an annual rate of just 650,000 in February. January sales soared to a 704,000 rate, but that was helped by the month's warm weather. February's decline is indicated by the 13.1% drop in single-family housing starts and by higher mortgage rates. February's expected sales rate would be the lowest in more than a year.

FACTORY INVENTORIES

Thursday, Mar. 30, 10 a.m.

Manufacturers most likely increased their inventories by 0.6% in February.

Factories had been stockpiling goods at a much faster rate. Inventories rose 0.9% in January and 0.7% in December. With unfilled orders still strong in the factory sector, the rapid buildup of inventories was probably intentional. Factory output in February was unchanged, so fewer goods were available for warehousing in that month.

FACTORY SHIPMENTS

Thursday, Mar. 30, 10 a.m.

The manufacturing sector will probably post a 1.1% decline in shipments for February, following a 0.3% increase in January. Durable-goods manufacturers have already reported a 2.5% drop in their shipments. Nondurable-goods sales probably rose a moderate 0.6%.



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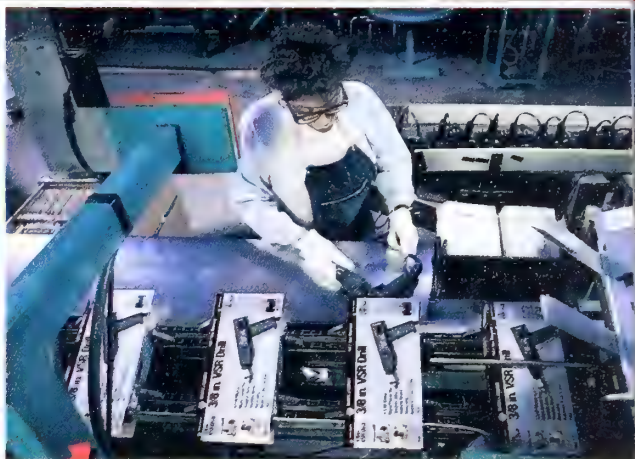
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REALLY CRACKING Oil prices have begun to rebound from last year's lows, gushing to \$20 a barrel



STICKER SHOCK Recent jumps in producer prices showing up in higher prices for consumer goods

THE ECONOMY

APRIL 3, 1989

INFLATION STAGES A COMEBACK

BUT IT'S A DIFFERENT BREED—SO IT MAY NOT SPIRAL OUT OF CONTROL

Inflation is back.

It isn't the inflation you remember from the 1970s: no shock of quadrupling oil quotes and zooming grain prices, no rapid buildup of inventories to beat price increases. And homeowners won't again see the doubling and tripling of house prices.

Still, inflation is back. And while today's inflation isn't likely to culminate in 20% interest rates and a steep recession, it's worrisome nonetheless. More and more economists expect that inflation, as measured by consumer prices, will top 5% this year, and many believe it could rise by 5.5% or more. That's up from 4.1% in 1988, 3.7% in 1987, and 1.9% in 1986, the decade's lowest rate. Most of the time, "inflation doesn't explode," says Robert Dederick, chief economist at Northern Trust Co. in Chicago. "It just gradually worsens and becomes more and more firmly entrenched."

'ON GUARD.' Just how entrenched it gets this time will depend on two things: how worried about rising prices Washington policymakers become and how strong the economy is in coming months. Outgoing Commerce Under Secretary Robert Ortner, for one, is troubled by the latest numbers, which show producer

prices growing at a 12.6% annual clip in the first two months of the year and consumer prices rising at a 6.1% rate. Like other economists, Ortner has concluded that prices have moved onto a higher plane. "We should be apprehensive, and we should be on guard," says Ortner. "We can't afford to let inflation get out of control."

Members of that inflation-fighting bastion, the Federal Reserve Board, certainly can't afford to let inflation get out of hand. But as usual, or perhaps even more than usual, the Fed is in a bind. A policy of gradual monetary tightening may not have slowed the economy enough, and now Fed governors and district bank presidents must decide whether to turn the screws tighter and risk recession (page 34). The repercussions could be global, as central bankers match U.S. rate increases to head off a higher dollar. European and Japanese officials are already worried about homegrown inflation. Now U.S. inflation is giving them more to fret about. But Bush Administration spokesmen maintain that the recent numbers were a fluke and inflation has peaked.

Granted, worries about inflation aren't universal. Edward Yardeni, chief econo-

mist at Prudential-Bache Securities Inc., while conceding that the underlying inflation rate has moved higher in recent months, is still betting that the consumer price index will rise 4% to 4.5% in 1989. Yardeni believes that enhanced global competition, more capacity expansion, and improving productivity will keep a lid on price increases. But right now, he says, there's a race between those forces and the end-of-expansion pressures that typically push prices up. For the moment, the latter are winning.

TEXTBOOK CASE. Indeed, the current inflation is shaping up as an almost classic late-cycle phenomenon. The economic expansion is in its seventh year, unemployment is at a 15-year low of 5.1%, and capacity utilization rates are still high, although the industrial sector is beginning to show some signs of cooling down (page 29). Wages have only recently come under upward pressure, but that's not surprising—the early moves on the inflation front tend to start elsewhere. This time, the first big push on prices began in late 1987, when crude-material prices started rising, thanks to growing demand from industries such as chemicals and paper. Last year those increases passed through to the intermedi-



LATE HARVEST The effects of last year's drought are being felt by supermarket shoppers



FEVER PITCH Both health care costs and drug prices are ratcheting upward

ate-goods level, on everything from linerboard to specialty steel. Now the sharpest increases are for finished goods like drugs and flatware, while crude-material prices fell in February.

That's some consolation, but it isn't entirely reassuring because catch-up pricing seems to have only just begun. We're a long way from the early 1980s, when a concerted round of inflation-fighting pushed the price indexes way down. At that time, says economic consultant Joel Popkin, "people stopped speculating on inflation. Companies were disabused of the notion that they could just pass prices along. A whole anti-inflation gestalt developed." Now, warns Donald Ratajczak of Georgia State University, resistance to price hikes is deteriorating.

Indeed, Aluminum Co. of America, which has about a 40% share of the market for the sheet aluminum used to make beverage cans, last year froze prices because it feared losing business to steel and glass. Now it's hiking prices on aluminum-can materials by 4% to 6%, and rivals Reynolds Metals, Alcan, and Kaiser are following suit. Meanwhile, Allegheny Ludlum Corp., the largest specialty steelmaker, is pushing stainless steel prices up because of the escalating cost of such raw materials as nickel and chrome. In March, the price for stainless sheet was up 38% from a year earlier.

DELAYED EFFECTS. Even the commodities that once produced price "shocks" for the economy aren't quite as well behaved as they were a couple of years ago. Food prices spiked recently, as some delayed effects of last year's drought showed up. Energy prices, meanwhile, have been rising from their

lows of last year. World oil demand outstripped the most optimistic projections, jumping 5.5% in the final months of 1988, and it's slated to grow about 2% this year. At the same time, supply has been tightening, thanks to OPEC and non-OPEC production cuts. Excess capacity should keep prices from rising much higher. But, observes Daniel Yergin, president of Cambridge Energy Research Associates: "Oil has been a major ally in the war against inflation. It's clear that this is changing now."

The price indexes are almost certain to look bad for the next couple of months,

certain whether the economy is at an inflection point or not. Cool down, however, it must. Says Roger Brinner, chief economist at DRI/McGraw-Hill: "The economy has been on a slow boil. Eventually, the food is cooked, and you've got to turn the heat off."

MILD RECESSION? Brinner, for one, sees a marked slowdown in growth beginning in the spring, with real gross national product rising only 1.5% in the final three quarters of the year. Others expect a mild recession later this year or early next, while some see sluggish growth and no recession. But few economists expect slow enough growth—or a recession deep enough—to restrain inflation. Some fear that a mixture of slow growth and rising prices, or stagflation, will mark the economy of the early 1990s.

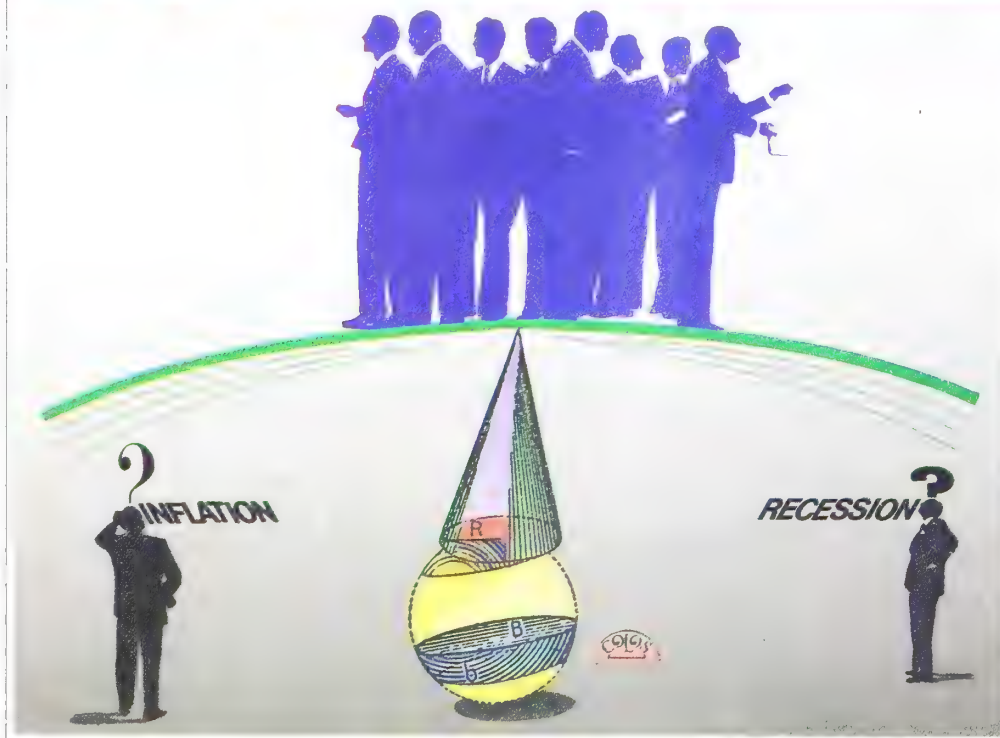
Right now, the inflation stakes just don't seem that great. But the fact that wages and prices aren't out of control shouldn't rub out all worries about prices—particularly since costs in some areas, notably health care, are rising sharply. Nor should the prospect of slower growth. Inflation is back, and, if truth be told, it never really disappeared. The last year that the CPI actually fell was 1955. Economists debate whether zero inflation is desirable or even attainable. But the goal of price stability is one every economist readily embraces. So, can we learn to live with 4% inflation? Or 5%? Or...? Probably, because in a sense we already have. But just like learning to live with the bomb, you've got to be extra careful.

By Karen Pennar in New York, with Howard Gleckman in Washington, Michael Schroeder in Pittsburgh, Mark Ivey in Houston, and bureau reports



if only because that big oil component hasn't yet been fully reflected in the numbers. Although domestic crude oil is now selling at \$20 a barrel, the February producer price index was based on a \$17-per-barrel price, while the February CPI was based on \$15 per barrel.

Whether oil and other prices will rise further depends most heavily on business conditions. Last year the economy confounded the experts. Real growth, even including the effects of the drought, came in at 3.8%, and economists busily started refiguring their estimates for this year. But the data for 1989 thus far are mixed, and nobody is



THE FEDERAL RESERVE

IT'S WAIT-AND-SEESAW TIME AT THE FED

Its policymakers will likely hold off on a new round of interest hikes

Richard F. Syron studied economics in the 1960s, when academic arguments raged over how long it took for monetary policy to affect the economy. When a central bank relaxes its grip on money, cutting interest rates to jump-start a slow economy, Syron was taught, "you see the benefits in growth long before you see any cost in inflation. The downside is, when you tighten, it's the other way around—the costs come long before the benefits."

Welcome to the downside, Mr. Syron. As the new president of the Federal Reserve Bank of Boston, Syron will cast his first vote in the Fed's policy-making Federal Open Market Committee (FOMC) on Mar. 28. He'll have to turn those abstractions into a concrete choice: Jack interest rates up now to head off burgeoning inflation, or hold off for a few weeks to see if the economy is slowing. The Fed has to decide which statistics best foretell the economy's future: the back-to-back 1% hikes in producer prices in January and February, or recent weak showings in auto sales, consumer spending, and factory output.

Odds are that Syron and his FOMC col-

leagues will vote to hold off on higher rates—for now. A year after they first turned their attention to the dangers of inflation, Fed officials are betting that their tighter grip on credit will soon show results. "I don't think we've seen all the effects yet of what we've already done," Richmond Fed Chief Robert P. Black says. Even Robert T. Parry, president of the San Francisco Fed and a leading FOMC hardliner, hopes that policy actions so far—capped by February's sharp hikes in short-term rates—"have set the stage for a slowing that will put the brakes on inflation."

But even if everything breaks the way the Fed would like, the surge in producer and consumer prices has moved the battle against inflation into a new and riskier phase. Financial markets are calling on the central bank to prove its resolve against inflation, while politicians stress the dangers of cracking down.

TOUGH CHOICE. Fed Chairman Alan Greenspan had hoped to head off this choice. Recognizing last spring that the economy was stronger than expected, he pushed the FOMC to tighten money. His fellow governors reluctantly went along,

and interest rates rose 2 points.

Now Greenspan faces a tougher situation—with fewer allies. The seven Washington-based governors, who have tended to caution on rate hikes, hold permanent votes on the FOMC, as does the New York Fed president. The other four votes rotate yearly among regional Fed presidents. Three 1988 hardliners—Parry, Black, and Cleveland's W. Lee Hoynes—won't be voting this year.

In hindsight, some critics argue that Greenspan missed his chance last year to crack down on inflation. "The Fed was never really restrictive in 1988," says New York bond-market consultant Leonard J. Santov. "They just went from easy policy to neutral."

But it's hard to buy that argument. Fed Governor Wayne D. Angell points out that the Fed's key measure of the money supply, has grown at an

annual rate of less than 4.5% for two years. "It's the first time since the 1950s that we've had such stable, slow M growth," he says. He and Fed Governor H. Robert Heller point out that raw-material prices fell in February. And the economic evidence in 1988 "didn't support the idea of tightening even more in an election year," says economist Nicholas Perna of Connecticut National Bank.

DIVISIONS. Now, however, the inflation danger is clear and present. With prices and wages suddenly climbing throughout the economy, the best the Fed can hope for is a brief "stagflation"—a economy that grows slowly while inflation gradually stabilizes on a higher, 5% to 6% plateau. Even to reach that dismal result, the Fed will face months of sharp divisions over whether to squeeze harder. The dangers of overtightening are obvious: The economy could plunge into a recession, and that could compound savings-and-loan and Third World debt problems. But delay carries risks, too. If the Fed lets inflation dig deep into the economy, the result could be a boom-and-bust cycle that brings both high prices and eventual recession.

Greenspan believes the Fed's job is to prevent that inflationary surge—and most of his colleagues agree. That means the Fed is willing to push rates even higher if the economy doesn't slow down. But the lag between tightening and the economy's response will make the job ever harder. The Fed needs all the skill and finesse it can command.

By Mike McNamee in Washington

BEATING TODAY'S INFLATION MEANS PLAYING NEW ANGLES

Strategies that worked in past price spirals may not work in the future

With inflation heating up, investors might recall past price spirals in plotting a new strategy. True, real estate and gold worked wonders a decade ago, but that doesn't mean they'll provide safe harbor today. Nor are stocks and bonds necessarily anathema. "I've never seen an economic cycle that's the same as the previous one," says Ian A. McKinnon, fixed-income investments chief for Vanguard Group. "There's something different and unexpected each time you go around." Here's the outlook for stocks, bonds, real estate, and gold.



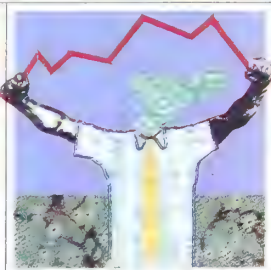
STOCKS

Stick to companies with built-in hedges

Stocks were once promoted as inflation hedges, but they lost that allure in the inflationary 1970s. Still, savvy investors can find stocks of companies that will prosper. After all, inflation gives some an excuse to pass on increased costs to customers and allows those with fixed-rate debt to pay off in cheaper dollars.

Remember the runup in oil and other natural-resources stocks a decade ago? They've been hopping lately. But Carne Grigoli, portfolio strategist for First Boston Corp., warns against relying on the same hand. "Then we were fearing inflation because of shortages of basic materials," he says. Today, high prices stem from capacity shortages in many industries that process raw materials. So the best bets, Grigoli believes, are in such industries as chemicals and paper where plants are running at full capacity.

Another tactic: Buy companies whose growth rate will far outpace inflation. They're often small niche businesses, such as software or specialized machinery. "If there's a market for their products or technology, such companies will do well," says Donald A. Herman, a managing director of William D. Witter & Co. Indeed, small-capitalization stocks outperformed the big names in the late 1970s.



BONDS

Short-term issues now offer a comfy cushion

Inflation decimated the fixed-income market a decade ago, when long-term bonds lost as much as 40% of their value. Now investors swear they won't get burned again. They price bonds so that real interest rates—the nominal rate less the inflation rate—are high, usually a 3-to-4 percentage-point spread. In the last big bout of inflation, bond yields actually fell below the inflation rate.

Today's high real rates offer bondholders some extra cushion against the erosion of purchasing power caused by inflation. But high real rates still won't protect them from capital losses if nominal interest rates continue to climb. So loading up on long-term bonds is for now a risky play.

Fortunately for investors, they can earn high real rates of return in the shortest maturities. The interest rate on three-month Treasury bills is currently 9.4%, while the consumer price index—used by many as a guidepost for inflation—is around 6%. The difference between the two, explains Gary P. Brinson, president of First Chicago Investment Advisors, "provides what is historically a very generous real return." And if rates continue to climb higher, investors will still get the opportunity to reinvest at higher levels.



REAL ESTATE

Most properties will barely hold their ground

In the late 1970s, buying a home was a sure bet to beat inflation. After inflation and tax deductions, borrowing costs were negligible. That allowed new buyers to pay even higher prices, steadily pushing up the housing market.

Then, in the mid-1980s, prices surged anew in many markets, fueled by a drop in interest rates.

But now prices are so high relative to annual household income—as much as seven times in metropolitan New York—that there's little untapped buying power left. Couple that with rising mortgage rates and it's hard to see runaway price increases in residential real estate. Of course, every market is unique. Although on average, prices will keep pace with inflation, real estate won't get you far ahead.

Commercial real estate is even less certain an inflation hedge nowadays. "Many, many markets are overbuilt," warns Larry Biehl of the investment firm Bailard, Biehl & Kaiser Inc. "It could take four years for supply and demand to reach an equilibrium that makes sense." Garnett L. Keith, vice-chairman of Prudential Insurance Co., is also wary. He warns that high vacancy rates can sting investors badly. The reason: Inflation will push costs up, but landlord-investors won't be able to pass them on by hiking rents as long as there's a glut of space.



GOLD

The metal's message: Don't worry

By now, you would expect that speculators would be furiously bidding up gold prices and people would be banging down coin dealers' doors. Instead, gold has barely budged. At \$395 an ounce, the yellow metal is 14% below its year-ago level, prices not seen since 1986, a year that saw the lowest inflation rate of the decade.

Why has gold lost its aura? For one, high real interest rates, which mean investors can buy short-term securities and preserve their purchasing power. Owning gold pays no dividend and actually may cost investors to finance and store. An increase in supply is also depressing the gold market. The runup in prices a decade ago spurred new mining ventures that have only recently come on line. Production last year increased 9% and is expected to grow similarly in 1989.

Investment adviser Biehl still believes in the role of gold "as a whip against inflation" and thus finds hope in the lackluster market. It may be telling investors that those threatening clouds of inflation will glide by with just a passing shower.

By Jeffrey M. Laderman in New York

Commentary/by Douglas A. Harbrecht and Paula Dwyer

ETHICS REFORM: THE TRICK IS TO KNOW WHEN TO STOP

Washington is in the throes of an ethics convulsion. Suddenly, the rules for officials are growing stricter, even prudish. President Bush's first act in office—the appointment of a government ethics panel—unleashed furies the White House never imagined. Bush's symbolic step may have backfired and cost him his choice of John G. Tower for Defense Secretary. The next victim could be House Speaker Jim Wright, under investigation for a variety of alleged misdeeds.

The ethical laxity of the Reagan years was bound to unleash a reform movement. But the danger is that, like most reactions, this one will go too far. If the reformers aren't careful, they'll end up chasing talented people away from elective office, appointed jobs, and civil-service positions.

The President's Commission on Federal Ethics Law Reform is recommending a raft of changes, most of which Bush will incorporate into legislation he will soon send to Capitol Hill. The commission's report offers a good starting point, but Congress must refine the changes to ensure honesty in and out of public service without requiring a vow of poverty. A few principles lawmakers should keep in mind:

■ **Keep it simple.** Ethics rules can become a quagmire. All too often, government ethicists write rules designed to prevent a recurrence of the last outrage. Such detailed rulemaking only makes it easier for lobbyists and others so inclined to find loopholes. It's better to cite clear, general guidelines and require officials to make full disclosure of potential conflicts. That way, a beefed-up Office of Government Ethics, the Office of Personnel Management arm charged with enforcing the requirements, can monitor disclosures and help people avoid conflicts.

■ **Be reasonable.** Congress should adopt the commission's recommendation that members of Congress and Hill staffers be banned from lobbying their former

employers for one year. The current maze of ban periods, which apply only to executive branch officials according to salary and levels of responsibility, should also be simplified.

The commission duly recognizes that some situations in the executive branch call for a two-year prohibition. These include cases where an individual had primary responsibility over an issue and retains particularly sensitive and

they were "substantially involved" in government. Come on. If people are banned from doing what they know best once they leave government, they'd never join in the first place.

■ **Don't penalize honest people.** Congress should follow the commission's recommendation to allow officials who must unload stocks or bonds to avoid potential conflicts to reinvest the proceeds without paying tax on any gain.

■ **Lawmaker, heal thyself.**

Congress must abolish the "honoraria" scam in which members supplement their income by giving \$2,000 breakfast chats for interest groups. In return, President Bush should recommend a 25% pay increase for Congress, judges, and top federal officials. This is more palatable than the 51% pay raise that Congress rejected last February after a public outcry.

The lawmakers also should close a loophole in campaign finance law under which 190 House



GOVERNMENT ETHICS: A SOLID FOUNDATION

- ▶ Keep the rules clear and simple
- ▶ Apply the same basic rules to all three branches of government
- ▶ Don't make the rules so stringent that they discourage the honest from entering government service
- ▶ Raise pay for judges, congressmen, and top federal administrators, and ban congressional honoraria

timely information. For example, the Commerce Dept. official responsible for setting quotas on Japanese auto imports could not lobby to change the quotas on behalf of a Japanese manufacturer for two years.

But lifetime bans are a mistake. Last year, President Reagan vetoed an ethics bill that barred senior government officials from ever "aiding or advising" outside parties on matters in which

members elected before 1980 are allowed to take leftover political contributions with them when they retire. A number of veteran members are building up million-dollar nest eggs.

■ **Parity is good, up to a point.** Bush's commission calls for the use of special prosecutors to investigate alleged wrongdoing by members of Congress. There's no need for that. Independent counsels help avoid situations where the executive branch otherwise would be investigating itself. And the Justice Dept. has never been shy about going after misdeeds on the Hill. The Wedtech probe is ample proof of that.

Above all else, Congress should remember that most forms of outrageous ethical behavior are already illegal. After all, top Reagan aides Michael K. Deaver and Lyn Nofziger were convicted for perjury and illegal lobbying, respectively, under existing laws. Federal ethics laws may need some fine-tuning, but Congress should be careful not to overreact to past excesses by putting present and future officeholders into ethical straitjackets.



ASSEMBLY AT IBM: THE STOCK TANKED BECAUSE WALL STREET HAD ESPECIALLY HIGH HOPES

A DOUBLE WHAMMY SPOOKS HIGH-TECH INVESTORS

But bad news from IBM and DEC doesn't presage a computer slump

Is the computer market headed for another sales slump? Industry watchers and investors began to wonder a few weeks back when Apple Computer, Microsoft, and Prime Computer announced that March quarter earnings would be below expectations. Now, wonder has turned to alarm after the big boys, IBM Corp. and Digital Equipment Corp., came forth with their own warnings.

Big Blue's stock skidded eight points in two days after a Mar. 17 disclosure of production problems on its biggest computer line. Five days later, DEC took a 10-point tumble when it told analysts its quarterly revenues would be \$100 million under projections. The double-whammy sparked a sell-off on a wide range of technology stocks. "Everybody is looking for a crack," says Standard & Poor's Corp. analyst Melanie McCrossen. They're all trying to see the first sign of a downturn."

HIP SNAG. Yet a slump isn't likely. Although higher interest rates could slow capital spending, and with it computer purchases, Wall Street had already been predicting mediocre growth in U.S. computer sales for 1989. And the events that spurred the high-tech sell-off seem to be problems that the various companies wrought on themselves. IBM, for example, is having trouble making a key microchip for its mainframes. That has de-

layed shipments. In fact, the very day it confirmed the chip snag, IBM raised prices for most products by 5%—hardly an indicator of slumping demand. At DEC, the problem is sluggish U.S. demand for its largest VAX minicomputers. But that's because customers are awaiting new models due out in the summer.

IBM tanked because Wall Street has had especially high hopes for it. The company had revamped its product line from top to bottom and appeared to be cutting costs. But IBM's story—that the delays caused by the chip problem would depress earnings for the year—made investors suspect that the company has even more bad news in its future. "IBM has lost its way," asserts Ulric Weil, an analyst with Weil & Associates. "It's stumbling around in the wilderness."

The biggest problem, as Prudential-Bache Securities Inc. analyst Rick Martin sees it, remains IBM's bloated cost structure. "The shift to desktop computing has happened much faster than IBM anticipated," Martin says. Meanwhile, IBM still has the enormous overhead it built up for selling mainframes. Although the company has reduced its pay-

roll by 22,000, redeployed thousands more to the sales force, closed up plants, and sold off major businesses, IBM's overhead has actually grown as a percentage of revenues (chart). That has analysts questioning Chairman John F. Akers' ability to reach his stated goal of boosting operating margins from the current 15% to its traditional 20%-plus level. "Cost-cutting will have to become a way of life for IBM," says Stephen Cohen of SoundView Financial Group Inc.

That's not as easy as it might seem. While the mainframe market is only growing by about 4% a year, mainframes and related products and services still account for 50% of IBM's sales and an estimated 70% of its profits. And IBM mainframes are under siege. In the past 15 months IBM has lost two points of market share in the U.S. to makers of IBM-compatible mainframe processors, according to market researcher Computer Intelligence, in La Jolla, Calif. Last spring, when Amdahl Corp. brought out an IBM-compatible mainframe that outperformed Big Blue's biggest 3090, IBM was forced to trot out a new high-end machine six months ahead of schedule. That, in turn, pushed Big Blue's East Fishkill (N.Y.) microchip plant into overdrive to make the necessary parts—which led to the chip problems that now are delaying 3090 shipments.

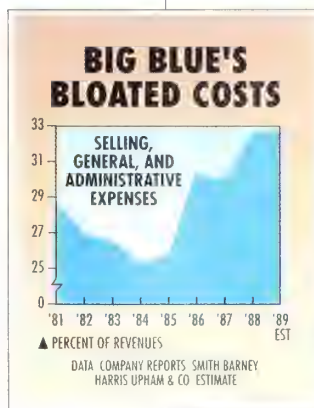
HITTING THE WALL. DEC is feeling a similar pinch—in part from IBM. Although its overseas business continues to grow rapidly, DEC's growth in the U.S. has hit a wall. "What DEC is experiencing now is what other minicomputer suppliers started feeling six months ago," says Donald Bellomy, an analyst with market researcher International Data Corp. "We

expected that growth in the minicomputer market this year would be mainly IBM's. The others are giving back the market share that they had been grabbing from IBM for the past few years." Without further domestic growth, analysts now regard DEC's cost structure as out of line. In fact, they have cut earnings estimates for the year ending June 30. Laura Conigliaro of Prudential-

Bache Securities started the sell-off in DEC by slashing her forecast to \$9 from \$9.65.

So DEC and IBM seem to have ready explanations for their disappointing news. That has done nothing, though, to assuage Wall Street, which will go on wondering if the big boys' simultaneous missteps are more than a coincidence.

By John W. Verity in New York



TIME-WARNER: THREE'S A CROWD

Bob Bass may stop the merger

That voice you hear from the back of the church? It sounds like an objection to the marriage of Time and Warner. Billionaire investor and sometime raider Robert M. Bass has amassed a big stake in Time Inc., and he's not happy with the company's wedding plans. Some fast money on Wall Street took that as a sign that Bass will try to topple the stock swap by making an offer of his own: Time shares on Mar. 21 leapt 7 3/4 points, to 119.

The Bass camp strongly hinted that the Fort Worth-based investor is prepared to make some serious trouble for Warner Communications Inc. Chairman Steven J. Ross and Time Chairman J. Richard Munro, the pair who jointly plan to lead Time Warner Inc. "I don't doubt his ability to do a deal that size," says a source close to Bass. What's more: "Bob doesn't make a run at something he doesn't think he could get done." And an investment banker who has worked with Bass isn't surprised that he might want to stir things up. "He, like everybody else, looked at Time with lust."

Bass has some powerful incentives to act. A source in the financier's camp says Bass has substantial holdings in Time—but disputes, without elaboration, reports that put the figure at 2%. If, as Bass is said to believe, the proposed stock swap gives Time to Warner shareholders for a song, then Bass would lose out in the merger. He is said to think that Time is worth about \$200 a share were the company to be broken up and sold in pieces.

FAIR SHARE. Moreover, Bass has amply shown that he's willing to speak up when management doesn't give shareholders their due. That was one reason Bass sued Macmillan Inc.'s management when it sought last year to restructure the publishing company to deter a raider—and keep for itself what seemed the more valuable pieces. British media mogul Robert Maxwell finally won the prize for \$2.5 billion. In 1987, Bass joined raider Carl H. Lindner and offered \$157 a share to beat Dudley S. Taft's attempt to take Taft Broadcasting Co. private at \$145 a share.

Bass can afford Time, which the stock market now values at about \$6.8 billion. Bass's junk-bond arm, Acadia Partners, could probably raise enough money to



BASS: THE BILLIONAIRE INVESTOR THINKS TIME INC. IS WORTH \$200 A SHARE IF BROKEN UP

make a credible bid. Acadia boasts assets of more than \$1 billion. And Bass will raise some additional funds from a deal announced on Mar. 21. A group of investors led by Acadia plans to sell the holding company for Spectradyn Inc. to financier Marvin Davis. Acadia could realize as much as \$50 million on the \$635 million deal for Spectradyn, which shows TV movies to hotel guests on a pay-per-view basis.

BIG DEAL. Bass probably couldn't swallow all of Time without borrowing and, perhaps, selling assets later to pay off acquisition debt. Last year he made his biggest offer ever when he bid \$1.9 billion for Macmillan. He had previously joined some Japanese investors to buy Westin Hotel Co. for \$1.5 billion, and he soon sold its most valuable property, New York's Plaza Hotel, to Donald Trump for \$410 million.

Wall Street has its doubters. Some investors believe Bass simply wants to stir up interest in the stock so he can make a fast buck. Or he may want to send a signal that he's ready to form an alliance if someone else makes an offer for Time. "It's what you might call a very interesting manipulation of the situation," says Guy P. Wyser-Pratte, an executive vice-president at Prudential-Bache Securities Inc.

Time and Warner both seemed to take the Bass news in stride. "The feeling of Time executives is that it's nothing hostile," a Time spokesman says. A Warner representative declined to comment on the gossip. Of course, that's the same reaction Time and Warner officials had before the rumors about their merger plans proved to be true.

By Kevin Kelly in Dallas and David Lieberman in New York

ADVERTISING

SAATCHI & SAATCHI: THE EMPIRE TREMBLES

A profit plunge raises doubts about the company's management

It was too good to last. After 18 consecutive years of record profits, mega-advertising agency Saatchi & Saatchi PLC dropped a bombshell: 1989 pretax profits will be lower than last year. Analysts predict they will fall about 25%, to \$166 million, from 1988 figures. The reaction was swift. Wall Street hammered the stock, knocking more than 18% off the price of Saatchi's American Depositary Shares.

The earnings surprise rattles the foundations of the Saatchi empire. Brothers Maurice and Charles Saatchi assembled the largest ad-agency holding company in the world, mostly through U.S. acquisitions. Then they added an array of management-consulting units in an effort to create an integrated package of business services. But managing these companies has proven tougher than the brothers thought. Major client defec-

ions from Saatchi's largest U.S. agency and slow growth at its consulting division have put an end to stratospheric growth. "They don't have any excuse," says Chris Akers, an analyst with London-based Citicorp Scrimgeour Vickers. It can only be fallible management."

Chairman Maurice Saatchi puts most of the blame on slow U.S. ad spending growth—but that's something all U.S. agencies are facing. The real problem at Saatchi is its failure to win new accounts. The company's key U.S. network, Saatchi & Saatchi Advertising Worldwide, lost close to \$97 million in domestic billings last year, including the JR Nabisco account. Because of SSAW's altering creative reputation, the agency as been able to make up for only about half that amount with outright new-account wins. New business from existing clients picked up the slack, but only enough to push up overall U.S. billings disappointing 3.6%, to \$1.74 billion. Roy Warman, joint chief executive of the advertising arm of Saatchi, admits: "We desperately need to get some growth back in the U.S. business." There is one bright spot. Another major Saatchi agency, Backer Spielvogel Bates Inc., posted a 9% U.S. billings gain, to 2 billion.

10 STEPS. The troubles extend to Saatchi's consulting arm, including Hay Group Inc., a human resources consulting firm Saatchi picked up in 1985. The business hasn't lived up to expectations. Saatchi had predicted that consulting revenues would hit 50% of the company's total by 1990. But the division has had trouble generating new revenues and keeping expenses down. This year consulting will account for only 26% of revenues, up from 22% in 1988.

That makes the acquisition trail Saatchi's best hope for meeting its ambitious consulting goals. Yet the company's increased debt, rising interest payments, and poor stock performance make a major purchase harder than ever.

So far, Saatchi hasn't come up with much of a plan to pull itself out of these oldtrums. Consulting chief Victor Millar talks about his "30 steps" to get Hay's revenues and margins up—but won't say what they are. Warman has signed on a new creative director and transferred Saatchi's new-business chief in Europe to the troubled New York agency. Cuts in corporate staff and consolidation of U.S. offices are supposed to help improve margins.

There's one area where the Saatchis show no sign of cutting back. According to the company's annual report, Maurice Saatchi and another unnamed top executive will receive a 25% raise—a figure that neatly matches the number that shocked the markets.

By Richard A. Melcher in London

SOME UNWELCOME SHOPPERS MAY DROP IN ON CARSON PIRIE

After a horrid '88, the retailer must boost margins—or risk a raid

Last summer was pure hell at retailer Carson Pirie Scott & Co. Its splashy arrival in the Twin Cities became a nightmare when inventory shortages left shoppers seething. Then a direct marketing unit collapsed under weak sales and bill-collection woes. The clincher: A test boutique catering to women executives fell flat. Last year's mess ended in a \$38.8 million loss, on sales of \$1.02 billion (chart). "We didn't have a lot of time to play golf," jokes Carson Chairman Peter S. Willmott.

He won't be hitting the links much this summer, either. On Mar. 15, Carson

gone private. "Any outsiders who wanted to get into the Chicago market would find a perfect entrée in Carson," reasons George Strachan, a Drexel Burnham Lambert Inc. analyst, who thinks Carson's stores and real estate could fetch \$20 a share, or about \$306 million.

RETURN TO ROOTS. None of this is lost on Willmott, who knows if he doesn't get Carson's act together soon, somebody else might. Carson's retail operating margins are running at 3% to 4% annually, far below the industry's 8% average. Unless those margins widen soon and turn red ink into black, Carson



BRIGHT SPOT: CARSON PLANS 64 NEW STORES THIS YEAR FOR ITS BOOMING COUNTY SEAT CHAIN

unveiled a management makeover in which Willmott will take direct control of the retail operation: Carson's chain of 33 department stores, its 385 County Seat jean shops, and its 23 Arcadia card-and-gift boutiques. Carson will divest CPS Direct Marketing Inc. and close Corporate Level, the Washington (D.C.) "power attire" women's shop.

An even bigger challenge may lie ahead for Carson, whose stock has swelled 17%, to about 14, since the start of the year. It's the T word—takeover. Carson is one of the last big retailers that hasn't been swallowed up or

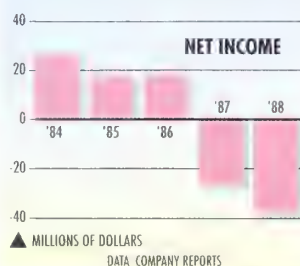
could find itself running from a raider.

Carson seemed healthy enough in 1983, when Willmott took over the top job after spending nearly a decade at Federal Express Corp., where he quickly rose to president and chief operating officer. Since his arrival he has jettisoned

Carson's specialty restaurant, airline catering, and floor covering operations—and taken the 134-year-old company back to its retailing roots. In 1987, Willmott paid Allied Stores Corp. \$150 million for the Donaldsons Inc. department store chain.

In Minneapolis-based Donaldsons, Carson

CARSON PIRIE GETS THROWN FOR A LOOP



hopes to find a way to expand its traditional Chicago role as a purveyor of middle-brow goods. Carson spent three months expanding Donaldsons' offerings from such designers as Liz Claiborne and Esprit and adding others, such as Geoffrey Beene. In July it reopened under the Carson name amid a \$1 million promotion. Comic Jay Leno even showed up to hawk Carson to Minneapolitans.

FIXING THE KINKS. But not even Leno could wipe the frowns off faces of irate shoppers when shelves grew bare. Carson blamed software bugs in its distribution system. Laments Willmott: "We were running out of stock at the same time we were creating a lot of hoopla."

The snafu hurt revenues, leaving Carson's Minnesota store sales about 10% below target. Archrival Dayton-Hudson Corp. seized on the bumbling start, adding several points to its commanding share of the Twin City retail market—which brokerage firm Piper, Jaffray & Hopwood Inc. estimates at 50%. The debacle in part prompted the resignation in January of Carson's retail chief, Dennis S. Bookshester, says a big Carson shareholder. Neither Willmott nor Bookshester would comment on the resignation.

To fix things, Willmott wants to go back to operating basics. He must get Carson's distribution and inventory control system running right—and he'll start by working out the kinks in the system's computer software. He also plans this year to reap the benefits of eliminating duplicative overhead at Donaldson's. The payoff would be handsome: A five-percentage-point improvement in operating margins could swing Carson back into the black from last year's \$2.01-a-share loss, estimates William Danoff, an analyst with Fidelity Investments, one of Carson's largest institutional holders.

HOT SEATS. Carson also hopes to keep benefiting from the hot growth of its County Seat jeans and casual apparel shops, which cater to 18- to 24-year-olds. Featuring such brands as Guess?, Bugle Boy, and Levi, County Seat's sales per square foot have jumped nearly 50% since 1983, to \$213. That may yet leave room for improvement. The Gap, a rival retailer, last year rang up sales per square foot of \$328. And County Seat plans 64 new stores this year.

Strolling through a County Seat outlet in Chicago's Loop recently, Willmott beamed at a flashy array of styles stacked neatly on display racks. "Teens have tons of cash," he notes. True enough. But Willmott must start generating some green for shareholders—and fast. Otherwise, he might soon find Carson on a sales rack of a different kind.

By Brian Bremner in Chicago

Commentary/by Frances Seghers

CALLING FROM THE ROAD SHOULDN'T BE HIGHWAY ROBBERY

What does Uncle Sam have against pay-phone customers, anyway? In the past few years deregulation has opened the \$3.5 billion public pay-phone market to a proliferation of privately owned phones that eat quarters or just plain don't work. It has also let newcomers compete with traditional phone companies for operator-services business—and customers have been complaining of price-gouging ever since. Now a federal judge has ruled that starting on Apr. 1, the seven regional Bell phone companies must open their 1.7 million public pay phones to all suppliers of long-distance phone service.

The ruling by U.S. District Judge Harold H. Greene sounds good, since it encourages competition. But his April Fools' Day plan could push rates more than 250% as high as those currently charged by American Telephone & Telegraph Co. Such pricing is already being seen around the country.

Some say Greene is only doing his job of enforcing antitrust law and slaying the old Bell monopoly. But his order reinforces a murky telecommunications policy that is failing the consumer. The Federal Communications Commission refuses to set pay-phone rates, preferring to leave such matters up to the states. A congressional bill that would force the FCC to review pay-phone rates is gaining support.

FAULTY REASONING. The Baby Bells have always routed their \$2 billion in pay-phone traffic to AT&T. Greene found this anticompetitive and wants phone companies to let businesses that lease pay phones, such as the local florist or saloon, choose a carrier. It's similar to an earlier ruling involving residential customers, which has led to a steep decline in rates since 1984.

But Greene's edict fails to reflect how the pay-phone market operates. Residential customers want the lowest-priced service, but those with pay

phones on their premises have a great incentive to hook up with higher-priced carriers, since these so-called alternative operator service (AOS) carriers pay higher commissions. Already, AOS companies such as International Telecharge, National Telephone Services, and Central have made significant inroads into pay phones owned by hotels and airports.

NO CHOICE. Customers are getting creamed (table). AOS commissions are simply tacked on to the price of a call. And a caller on the road often has no choice of pay phones or any idea which

carrier is handling the call or at what price. Even worse, about 90% of calls from public pay phones are charged to credit cards, with the bill arriving long after the call is made. Many AT&T, MCI, and U.S. Sprint card users have been unwittingly charged higher rates because they didn't know the pay phone they had used was being serviced by an AOS. Faced with a national policy that tells AOS companies, in effect, to

"get it while the gettin' good," Florida, North Carolina, and other states are heeding cries from consumers to crack down.

Greene knows his plan is flawed. His Oct. 14 decision noted that the national phone network can't currently handle the ideal solution—letting customers reach their carrier simply by dialing 0 plus their card number. But the FCC plan would only complicate things. It calls for AOS companies to identify themselves to callers and, if asked, give their rates or pass the customer on to another carrier. Says Representative Jim Cooper (D-Tenn.): "Most [callers] aren't rocket scientists, and the FCC shouldn't expect them to be."

Cooper aims to fix things through a bill that would force the FCC to review AOS rates and, if necessary, set nationwide pricing. If enacted, the legislation won't reverse Greene's decision. But it should keep a lid on pay-phone rates.

PAY PHONES: HOW CHARGES DIFFER

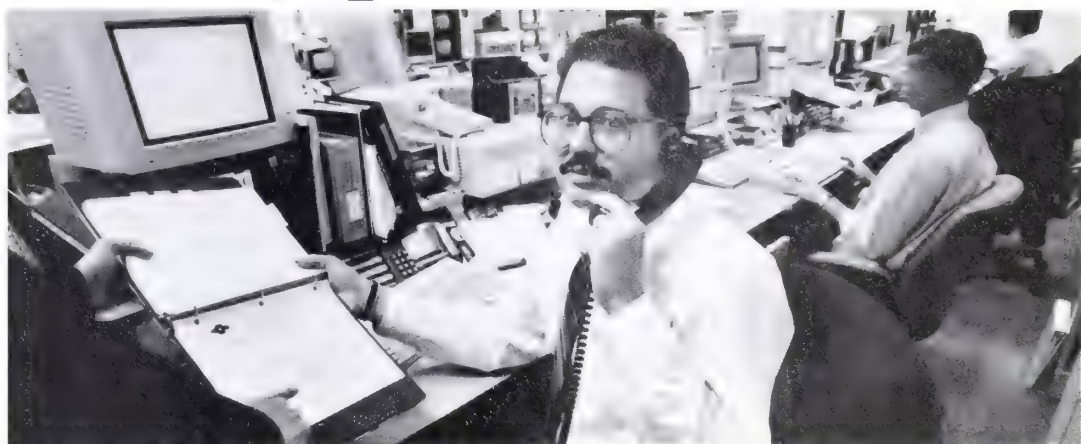
Average charges for a seven-minute call within 500 miles at business day rates

	Bell Calling Card rates	Person to person rates
AT&T	\$1.86	\$5.36
NTS*	3.68	5.43
ITI*	4.93	6.88
CENTRAL*	5.39	5.39

*Rates for National Telephone Services, International Telecharge Inc., and Central Corp. exclude possible surcharges of 50¢ to \$2.50

DATA: TELECOMMUNICATIONS RESEARCH & ACTION CENTER

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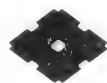
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A MOUNTAINOUS LOSS IN WEST VIRGINIA

Folks are up in arms over a \$300 million hit on a state investment fund

In 40 years in West Virginia politics, Democrat A. James Manchin has enjoyed voter support as he rolled through several government posts and on to two terms as state treasurer. But that may not be enough to save Manchin from the fallout of a \$300 million loss in the state Treasury Dept.'s \$1.2 billion Consolidated Investment Fund (CIF).

Making it all the more unseemly, state

ments in violation of state guidelines.

In the center of it all is the 62-year-old Manchin. He says that he has no intention of quitting and will fight the lawmakers' efforts to oust him. Manchin can point to legislative auditors, who concede that under his stewardship, CIF made more than it lost. "I am a West Virginia patriot and public servant," Manchin insists. "This is the only state

Trouble hit in 1987, when CIF suffered a \$202 million loss. Interest rates soared that April, and CIF managers saw their portfolio, chock-full of long-term, fixed-income securities, get hit. The reason: Higher rates inevitably mean lower bond prices. In an attempt to make up the paper loss, CIF's managers gambled that rates soon would fall. So they snapped up a bunch of short-term Treasury bills, financing the purchases mostly with \$11 billion in reverse repurchase agreements. Those so-called "reverse repos" effectively meant that CIF was borrowing money with its assets as collateral.

But rates kept soaring. So when it came time to settle the reverse repos, CIF had to raise money by selling off its Treasuries at a huge loss. The state attorney has yet to decide whom to sue.

But among the dozens of brokerage firms involved are such big names as Goldman Sachs and Morgan Stanley. The firms declined to comment.

FAT PAYOUTS. Worse yet, CIF began paying out to participants higher dividends than the fund was earning, dipping into its capital to do so. "It was mismanagement to say the least," charges Alison E. Patient, an attorney for the state House Finance Committee. News of the losses in December prompted a run on the fund, which remains solvent. State agencies are required to keep money in CIF. Not so town governments, nearly all of which have taken their money and walked.

Legislators, who are stuck with trying to clean up the mess, want Manchin's scalp. A legislative audit accuses Manchin's office of filing false statements about the fund's fiscal health, of taking risky trading positions far above legal limits, and of generally failing to invest prudently. Manchin blames his top lieutenant, former Associate Treasurer Arnold Margolin. Margolin blames his aide, former Investments Director Kathy Lester, for authorizing trades without his O. K. Lester says Manchin and Margolin both knew all along. Manchin also notes that it is the three-member state investment board—the governor, state auditor, and, as state treasurer, himself—that is officially responsible.

In the end, though, it may be taxpayers who will suffer. But lawmakers already are aiming to ensure that next time CIF deals with Wall Street, it gets a little professional advice first.

By Gregory L. Miles in Pittsburgh, with Topper Sherwood in Charleston, W. Va.



STATE TREASURER MANCHIN: THE LEGISLATURE IS THREATENING TO IMPEACH HIM FOR MISMANAGEMENT

lawmakers and Manchin are blaming one another—and almost anyone else they can think of. CIF, which under Manchin eschewed Wall Street advisers, lost most of the money in 1987. But the bad news didn't come to light until last December—a month after Manchin won reelection. Now the state House of Delegates is set to vote to impeach Manchin. If that motion carries, the Senate would then vote on whether to remove him from office.

'BAD LIGHT.' That's just the beginning. The Securities & Exchange Commission and the Justice Dept. are investigating CIF. And to recoup much of the loss, the state attorney's office plans to sue the big brokerage firms that handled the fund's trades. Among the complaints: Brokers knowingly sold CIF risky invest-

where you can be accused of making a profit."

As is often the case, this sad little tale had a happy beginning. In 1985 and 1986, Manchin persuaded town governments to invest their fire department, police, and other pension funds in CIF along with assorted funds from state agencies. Assets soared and, for a time, so did profits. Everybody was pleased.

The fund began paying participants higher dividends than it was earning, dipping into its capital to do so

"We're Japanese bankers."



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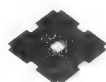
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EDITED BY HARRIS COLLINGWOOD

DRUG TESTING PASSES A MAJOR EXAM

► The Supreme Court handed the Bush Administration's war on drugs a major victory on Mar. 21 when it upheld mandatory drug testing for U.S. Customs Service workers and railroad employees. The justices said the government's interest in fighting illegal drugs outweighs the privacy interests of workers who are responsible for public safety and law enforcement.

Experts say the rulings will encourage increased testing in the private sector as well. The Drug-Free Workplace Act of 1988, which requires government contractors to ensure that their employees are not using illegal drugs, went into effect on Mar. 18. The law doesn't force contractors to randomly test employees. But the Defense Dept. is expected this spring to begin requiring almost all of its contractors to implement testing programs or be cut from the bidding process.

SALOMON HELPS KELLY BAG ENVIRODYNE

► Donald Kelly is back. After a recent abortive bid for Ohio Mattress, the former chairman of Beatrice has teamed up with Salomon Brothers to buy Envirodyne for \$751 million in cash. The Chicago-based maker of sausage casings and plastic cutlery, with strong market shares and cash flow, will likely serve as a vehicle for Kelly's future acquisitions. The deal also may enhance Salomon's reputation as a merchant banker. The firm has been trying to prove itself since deals with Revco and TVX went awry.

MICROSOFT VS. APPLE IS CLEAR FOR TRIAL

► Will Apple Computer and Microsoft step out of the ring before the fight gets too

bloody? Apple won the first round in its copyright lawsuit that charges Microsoft with imitating the "look and feel" of the Macintosh computer. On Mar. 20 a federal judge cleared the way for a full trial by ruling that Microsoft's 1985 license from Apple was not broad enough to fully cover later versions of its popular Windows program.

But the risks of a trial are so high for both that they may settle out of court. A trial could cause costly delays and require major changes in Microsoft's program. And Apple risks losing exclusive control over its pioneering display technology. If it goes to trial, the landmark case will help determine which companies will dominate the personal computer market in the 1990s.

COLEMAN IS NOW IN PERELMAN'S CAMP

► New York investor Ronald Perelman is adding camping gear to his grab bag of consumer products. On Mar. 20, Coleman accepted a \$74-a-share bid from Perelman's MacAndrews & Forbes Holdings. The \$545 million acquisition of the Wichita-based maker of lanterns and outdoor equipment fits Perelman's pattern of buying companies with leading brand names, including Revlon cosmetics and Marvel comic books.

WELL, MATTRESSES DON'T PAY INTEREST, EITHER

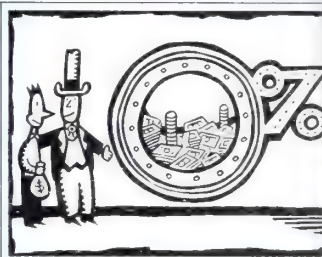
Texas bankers got into trouble partly by boosting the rates they paid on interest-bearing accounts. But at least one Texas bank avoided that problem in a way other bankers could envy—but almost certainly not match. D'Hanis State Bank in D'Hanis (pop. 760) simply doesn't offer any interest-bearing accounts. The bank, with \$1.5 million in deposits, only provides plain checking accounts. With virtually free money, the bank's return on assets averages 4%—five times the industry norm.

D'Hanis is a study in fiscal anthropology. The farming community located 50 miles west of San Antonio has always had just one bank, and that outfit has never paid interest. The bank is housed in an old wooden building with a rail for tying up horses. Tellers peek from behind gold grills. But why don't depositors demand interest? Says President Sam Moss: "Three generations of folks don't miss something they never had."

The deal comes a month after Coleman Chairman Sheldon Coleman, grandson of the founder, proposed taking the 90-year-old company private at \$64 a share. MacAndrews' offer increased Coleman's stock price 4½ points, to 73 on Mar. 22. Coleman earned a record \$24.5 million on sales of \$657.9 million last year.

A FRUSTRATING WEEK FOR U.S. PROSECUTORS

The government struck out on Mar. 22 in its first securities fraud case based on testimony by Boyd Jefferies. Jurors forced a second mistrial after 12 days of debating

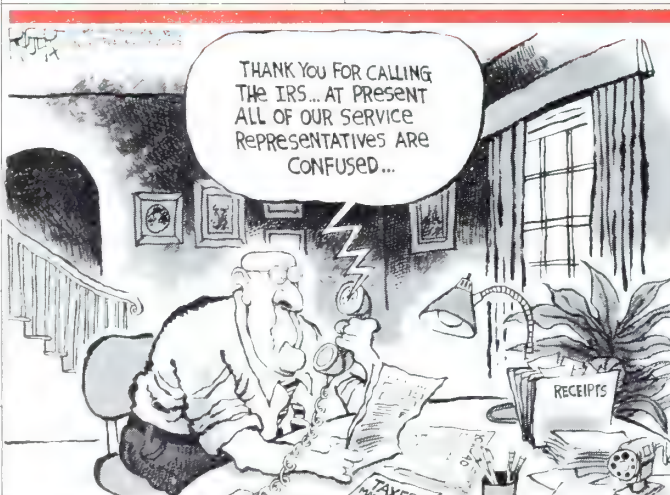


criminal stock-manipulation charges against GAF Corp. and its vice-chairman, James Sherwin. Acting Manhattan U.S. Attorney Benito Romanos now must decide whether to seek a retrial. Awaiting his decision are investor Salim Lewis and raider Paul Bilzerian, whom Jefferies also has fingered.

The week wasn't a total loss for prosecutors. The U.S. won a perjury case against Lisa Jones, a trader for Drexel Burnham Lambert, related to fraud charges against Princeton/Newport Partners.

THRIFT CREDITORS CAN TELL IT TO THE JUDGE

► Creditors of the hundreds of thrifts that enter federal receivership each year got good news from the Supreme Court. On Mar. 21 the justices ruled that creditors can take their claims to federal court instead of enduring the Federal Savings & Loan Insurance Corp.'s asset-disposition procedures. The FSLIC, itself a major creditor of failed thrifts, has been assuming the sole power to handle competing creditors' claims since 1985. The ruling could unleash a flood of lawsuits against the FSLIC.



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❖ **Money for Park Avenue Air**

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❖ **Don't Be Up in the Air**

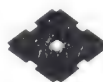
We've been helping and advising Japanese institutions and individuals on everything from plant and shopping center site location and leasing to personal real estate investments. If you have a real estate question, talk to us. Don't be left up in the air.

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IS BUSH PUTTING SCIENCE ON THE BACK BURNER?

Scientists had high hopes for the new Administration. After all, candidate George Bush repeatedly emphasized his commitment to science and technology—and vowed to make his science adviser a member of the Cabinet. White House Chief of Staff John H. Sununu, who holds a doctorate in engineering from the Massachusetts Institute of Technology, also professes to have a burning interest in the area.

But two months after Bush's inauguration, the science adviser's seat at the Cabinet table is empty. One reason is that some potential candidates worry that Sununu may have too much influence over the job. "There's a great potential for gridlock with Sununu," says one congressional staffer. Another problem is fear that the budget-strapped President won't give his science adviser the resources—or the clout—that's needed. "We're worried about the impression being given of a lack of interest," says a staffer on the House Science, Space & Technology Committee. "The job is obviously low on the totem pole in the White House."

The slow start is having consequences. Science and technology posts in government agencies and departments are being filled without the adviser's input. "The longer the delay, the less control the adviser will have," says Robert M. Rosenzweig, president of the Association of American Universities. **GROWING RESTLESS.** Indeed, a science adviser might make a difference in an ongoing trade dispute over which the Administration is deeply divided. It can't decide what restrictions to place on the uses of technology that General Dynamics Corp. wants to sell Japan for use in the FSX fighter airplane. "Japan is eating our lunch while we are floundering around on issues like the FSX," says Lewis Branscomb, a former IBM research chief now at Harvard University's Kennedy School of Government. "We haven't even begun to lay in place a strategy to bolster U.S. industrial competitiveness."

Both the science community and Congress are growing restless at the lack of action. The White House isn't commenting on the delay, but a majority of science committee members signed a polite but pointed letter to Bush asking that someone be nominated for the job "as soon as possible." And the mood

in science policy circles is grim, says Branscomb. "Despair wouldn't be a bad word for it."

Science organizations are reluctant to complain too loudly, especially since other key Administration posts remain unfilled. "Important as we think science is, we understand that it's not at the top of everyone's list," says Rosenzweig. And at least some science policy mavens are willing to look on the bright side. "If there's any reason for hope," says Ken Kay of the Council on Research & Technology, "it's the thought that Sununu is taking his time to make the right choice."

By John Carey

THE GOP'S NEW WHIP REALLY KNOWS HOW TO LASH OUT

The revolution is over for new House Minority Whip Newt Gingrich (R-Ga.). For the remainder of the 101st Congress, his biggest challenge will be proving to President Bush, GOP congressional leaders, and House Democrats that he's ready to make the big move from bomb-thrower to leader.

Gingrich, a 45-year-old former history professor, has spent his 10 years in the House as a guerrilla fighter, expressing the intense frustration Republicans feel after their 35 years as a minority in the House. Privately, most Republicans say that the man Gingrich defeated on Mar. 22, Edward R. Madigan of Illinois, was more qualified to be whip. But Minority Leader Robert H. Michel (R-Ill.), who backed Madigan, put it best: "There's this feeling we need to do something dramatic and different."

If anyone can do it, the blustery Gingrich can. His personality and temperament are like Tigger's in *Winnie-the-Pooh*. But Democrats still run the show—and they despise him. "He can make life hell for the Democrats," predicts political scientist Larry J. Sabato of the University of Virginia. "But he'll probably make life hell for the Republicans, too."

By Douglas Harbrecht

CAPITAL WRAPUP

SMOKING

It looks as if the latest way to get cigarette ads onto television is going up in smoke. In 1971, Congress banned tobacco ads on any electronic medium regulated by the Federal Communications Commission. Recently, however, cigarette commercials have been turning up on sets installed in stores to hit shoppers with advertisements or with "how-to" information. The programming is often sent directly to stores via long-distance phone lines. In response to complaints from health groups, the FCC ruled that such programming comes under its regulatory purview. The FCC can't ban the ads outright. It

has referred any enforcement action to the Justice Dept. But the commission's action is likely to discourage stores from running tobacco ads.

CONGRESS

They don't call Representative Richard A. Gephardt "Dickie Do-Right" for nothing. Hoping to keep his national reputation alive after his failed Presidential bid, the Missouri Democrat sent reporters a fat packet of press clips describing his accomplishments in Congress. To make sure there was no hint of impropriety, the customary free congressional frank on the envelope was covered with \$1.05 worth of postage stamps.

PUBLIC OPINION

In the old movie *Magic Town*, pollster Jimmy Stewart finds a town whose citizens' views perfectly reflect national opinion. Ever since President Bush said that a telephone chat with a friend in Lubbock proved how well his Administration is doing, the West Texas city of 200,000 has been trying to establish itself as a latter-day Magic Town. It has started a "D. C. Phone Home" ad campaign to promote economic development and to boost Lubbock as the source of down-home views on national events. But Lubbock should be careful. In the movie, sudden celebrity leads to the ruin of the town of Grandview.

The first in a series to help set the record straight.

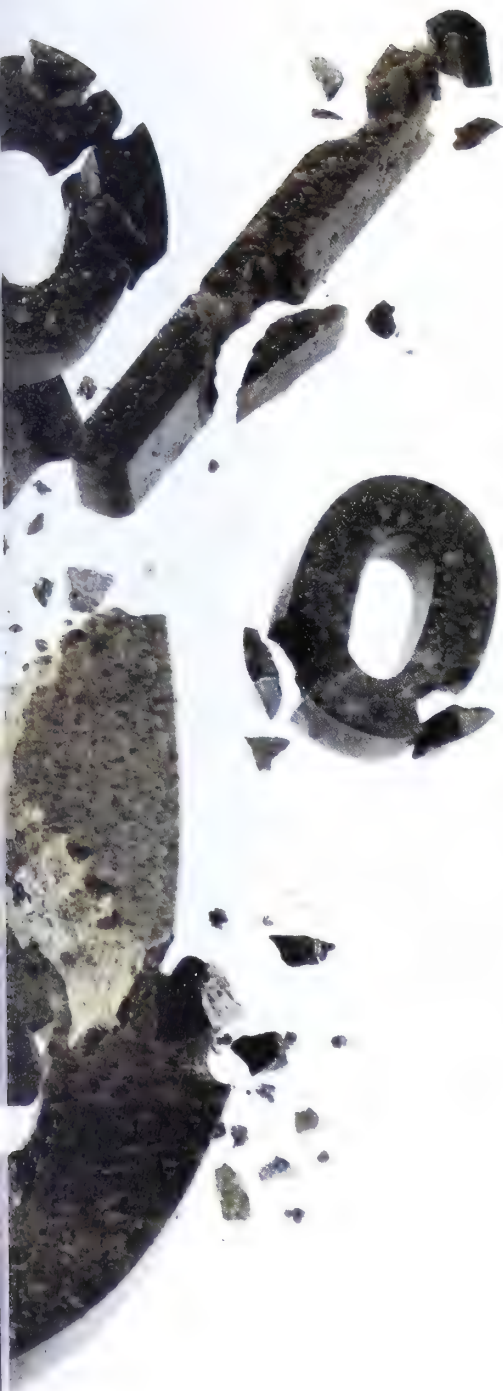
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ONE TOUGH HOMBRE

CAN PRESIDENT CARLOS SALINAS REMAKE MEXICO?

Sitting in his elegant offices in Los Pinos, the presidential mansion in Mexico City, Carlos Salinas de Gortari is in a good mood. Laughing often during a 40-minute interview with BUSINESS WEEK in mid-March, Mexico's new President banters about the importance of studying Machiavelli before becoming head of state.

These days, Mexicans rarely see this lighter side of Salinas. For in his first 100 days as President, the 41-year-old economist has shown that he is one tough hombre. He has already pushed through an unpopular austerity program to battle inflation, and he upset business with a 2% tax on assets. Then, venturing where no President before had dared, Salinas sent the army into a firefight to round up powerful oil-union bosses on corruption charges. Weeks later he tossed four stockbrokers into the same jail for fraud. And amid carefully planted whispers of a debt moratorium, he dispatched negotiators to Washington with orders to cut Mexico's bills in half. When they returned with the Bush Administration's Brady Plan to forgive some Third World debt, Salinas took credit for the breakthrough.

"Some days have seemed eternal," Salinas allows. "But if I can make the additional effort, my colleagues have to make it, too." Indeed, Salinas works 16-hour days and expects his staff to do the same. When they get sick, says a former campaign aide, he gives them "one hour to get better." Still, staffers lavish praise on the President. His modernization cause is theirs.

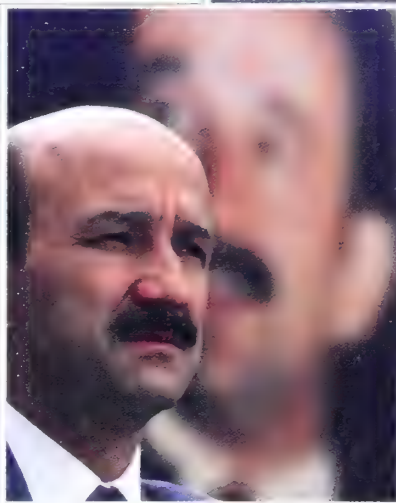
ASIA-STYLE. The former Budget Minister has clearly won over Mexico's elite. Large numbers of well-trained young Mexicans in business and government share his dream of converting Mexico into an Asian-style powerhouse on the U.S. border with booming factories and cheap labor. This means opening the door to foreign capital and pushing Mexican manufacturers into world markets while aggressively selling off dozens of state-run businesses, from the telephone company to the airlines.

But modernizing Mexico will require more than muscle-flexing. Salinas must also lead increasingly hostile and distrustful workers who have little in common with the professionals. Millions of Mexicans don't believe in his all-work, no-siesta cause. They only see Salinas making Thatcher-style reforms that promise to shut factories, crush unions, and hold down wages. Pay now and collect later, when the economy grows, he advises, warning that "rises in real salaries are going to have to be gradual."

Salinas' conservative policies have won him kudos from executives, and U.S. policymakers say he's a breath of fresh air. But the young President is the first in 50 years to face strong opposition. Last July, in Mexico's closest Presidential election ever, Salinas won his six-year term with just 50.7% of the vote. Many still charge that fraud put him over the top.

Today, large groups of Mexican workers, having lost half their buying power this decade, aren't swallowing his economic medicine. Thousands have taken to the streets demanding pay hikes. Teachers, who earn only \$150 a month, have shut down Mexico City schools and jammed streets with massive demonstrations. Their banners vilify the President, whose shiny pate and prominent ears lend themselves to caricature. In the shanties of Mexico City, a masked man called Superbarrio, a symbol of Mexico's underclass, rallies growing numbers of the poor against Salinas and his Institutional Revolutionary Party (PRI).

The next three months will be crucial. Foreign reserves are running dry, and a fragile anti-inflation pact of wage and price controls is due to expire this sum-



A BREATH OF FRESH AIR

IN HIS FIRST 100 DAYS IN OFFICE, SALINAS PUSHED THROUGH AN UNPOPULAR AUSTERITY PROGRAM, SLAPPED A 2% TAX ON BUSINESS ASSETS, AND SENT IN THE ARMY TO ROUND UP CORRUPT UNION BOS-

mer, just in time for a series of tough state and municipal elections. If the economy falters this spring, a rupture between the PRI and the unions that sustain it could bring Salinas' modernization project crashing to the ground. One surge of capital flight could lead to Brazil-style inflation and upheavals à la Venezuela. Economic disaster could push new waves of illegal immigrants into Texas and California. "Salinas has been much stronger than we anticipated," says one Bush Administration Mexico specialist. "But six months from now, I just don't know."



**MANY MEXICANS
AREN'T BUYING
SALINAS' PLAN.
TEACHERS HAVE
SHUT SCHOOLS AND
JAMMED TRAFFIC
ARTERIES WITH
MASSIVE PROTESTS**



**SALINAS HAS WON
KUDOS FROM
MEXICO CITY'S
YUPPIES AND FROM
WASHINGTON. BUT
HIS PARTY IS UNDER
FIRE IN THE POOR
BARRIOS**

To win the broad support he needs, Salinas must show he can deliver for the nation as a whole. Striking at the bogeyman of foreign debt—a staggering \$100 billion—is his best hope. Venezuela inadvertently gave him a hand in early March when riots against austerity broke out here. With hundreds left dead, U. S. policymakers got a powerful reminder of the powder keg across the Rio Grande. Within 10 days, Treasury Secretary Nicholas Brady had unveiled his proposals for reducing some Latin debt. Although Mexico's first in line, there's still a lot of haggling ahead. The negotiations "cannot go on for too many months," warns Salinas. The clock is already ticking. Thanks to

massive tariff reductions it made 18 months ago to prod domestic industries, Mexico is inundated with imports. Vendors in the Mexico City metro and at busy intersections sell M&Ms from the U. S.; supermarkets carry Sony TVs and butter from New Zealand. The upshot: a trade deficit topping \$200 million a month (charts).

Foreign reserves are sinking so fast that by July, Mexico may no longer be able to pay its \$11 billion in annual interest payments. Investors at home and abroad are holding on to their wallets until they see the Salinas program stick. Squeezed by price controls, businessmen are threatening to bolt from the anti-in-

flation pact. Meanwhile, the grass-roots clamor for long-overdue social spending is growing. "There's going to be a response by the people in these next few months," warns Patricia Olamendi, an opposition representative in the National Chamber of Deputies. "They can't take much more."

IRON-FISTED. To tide it over, Mexico might apply for a short-term loan from Washington. But a loan just to pay back interest would be viewed as a failure in negotiations. If Salinas limps into July without a decisive win at the debt table, his party is likely to fall to unprecedented defeats in state elections this summer. "The PRI may come in third place in some of those

elections," says Luis H. Alvarez, president of the conservative National Action Party (PAN).

While opposition leaders on the right and left smile, U.S. officials express concern. In a February newspaper interview, Central Intelligence Director William H. Webster labeled Mexico's political situation "fragile." Although Congress is likely to grant Salinas a honeymoon from outbursts over drugs and immigration, these bugaboos are certain to resurface. And President Bush showed his concern when he named as U.S. Ambassador John D. Negroponte, a security expert whose career includes service in hot spots from Vietnam to Central America.

Salinas isn't likely to waver if Mexico grows hot. He has shown a readiness to strike at his enemies with every weapon in his arsenal. People no longer question his resolve—only his motives. Says Rafael Moreno Valle, an investment banker in Mexico City: "If Salinas is doing all this to modernize Mexican society, then it is good. If it is just to consolidate his power, it's bad. It's too early to tell."

Even so, Salinas' iron-fisted tactics are nothing new in Mexican politics. Presidents have long banished their rivals to distant posts and thrown enemies into the slammer. Benito Juárez, Mexico's great 19th century President, summed it up neatly: "For my friends, grace and justice; for my enemies, the law." Salinas laughs when recalling the quote: "It's one of Juárez' maxims that Mexican politicians always keep in mind."

PRIVATE AMBITIONS. Salinas learned early political lessons from his father, Raúl, a former Cabinet secretary and presidential aspirant. The trick, he saw, was to hitch onto a rising star, serve him faithfully, and keep his ambitions to himself. He picked de la Madrid and rose with him into the Cabinet. Speculation before the 1988 elections centered on flashier possibilities, but Salinas quietly pursued alliances. He also tailored his appearance to the high office, replacing glasses with contact lenses, trimming the droop off his moustache, and banishing the sparse hairs from the top of his head. In October of 1987, de la Madrid chose the new, presidential-looking Salinas to succeed him.

Like Soviet leader Mikhail S. Gorbachev, Salinas inherited a "revolutionary" government collapsing under its own weight. Mexico's costly and far-reaching bureaucracy is often compared with the Soviet model, and its state-run industries are sometimes seen as overstaffed and inefficient as the Russians'. That means Salinas, like Gorbachev, must hack at the very structure that holds him in power. In Mexico, it's called *Salinastroika*.

To succeed in this precarious task, Salinas



MASKED MAN: IN MEXICO CITY, SUPERBARRIO RALLIES THE POOR AGAINST SALINAS

nas needs allies among the very people who turned out in droves against the PRI last July. He must woo them back to the fold with economic prosperity, and to do that, he needs loans from Washington. He's worked to win U.S. support by intensifying Mexico's war on drug traffickers and lending a hand to U.S. immigration agents. He has also more receptive to U.S. concerns about Central American insurgencies than were his predecessors, say U.S. diplomats.

With each bow to Uncle Sam, Salinas pays a political price at home. Critics such as Jorge G. Castañeda, co-author of *Limits to Friendship: The United States and Mexico*, accuse him of selling Mexico's sovereignty for debt relief. "His only constituencies are private business and the U.S.," maintains Castañeda.

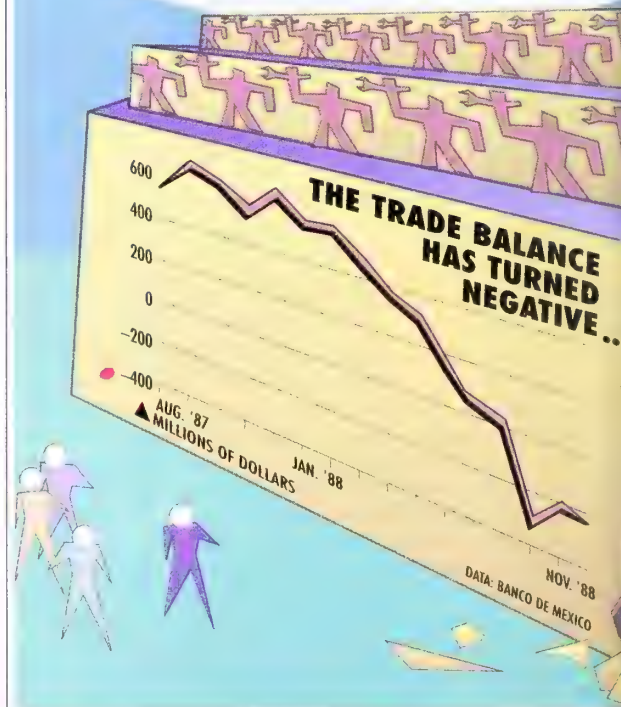
Equally troubling to the left is the economic program that Salinas launched as de la Madrid's Budget Secretary. The government has slashed spending in the past six years by 12% of gross national product,

promoted goods exports from \$4.8 billion in 1982 to \$14 billion last year, and hammered down inflation to 25% from a peak of 160%. But with one million Mexican entering the work force each year, the country has barely grown economically since 1981. Hidden unemployment is estimated to exceed 40%. Masses of Mexican make ends meet by driving gypsy cabs, eating fire and, increasingly, stealing cars and burglarizing homes.

Now the President is telling his powerful Washington friends that he needs \$7 billion a year for five years to sustain a recovery. Bankers and diplomats gasp at this amount. But Mexico has foregone even basic maintenance, from school rooms to oil rigs, since the oil market crashed. Petróleos Mexicanos (Pemex), for example, needs \$15 billion over the next five years just to keep production from falling.

What doesn't come from debt relief will have to come from private investment. Mexico naturally looks to the U.S., whose companies now account for two-thirds of its foreign investment. Ford Motor Co. and Chrysler Corp. are the country's No. 2 and No. 3 exporters, after Pemex. And more than 1,000 U.S. companies run *maquiladoras*, across-the-border plants that import parts and supplies and re-export everything from toys to computer keyboards.

MEXICO'S SHAKY FOUNDATION



Mexico wants more investments down-country. For starters, the government is offering dozens of concessions in the telephone business. Motorola Inc., American Telephone & Telegraph Co., and a host of smaller manufacturers are interested in cellular phone concessions. US Sprint and MCI Communications Corp. are among companies that could pick up long-distance business.

The Japanese are also interested in Mexico because of its proximity to the U.S. Some 25 *maquiladoras* in Tijuana are Japanese-owned. Honda Motor Co. makes motorcycles in Guadalajara, and Nissan's Cuernavaca factory turns out Mexico's most popular car. But for now, most Japanese are keeping their yen close to the border. They complain about the potholed highways, electricity failures, and spotty telephone service. "How could I make a computer down here and then put it on a truck and send it over those roads?" asks one Japanese diplomat. "It would arrive in a thousand pieces."

The Japanese also lament Mexico's quirky

foreign-investment law. On paper, though not always in practice, the law limits foreign ownership to 49%. Now, Salinas' young Commerce Secretary, Jaime Serra, is supposed to end the guesswork. "We're putting it all in black and white," says the Yale-educated economist. Still, few expect a reversal of the 51-49 law. Some in-

1989 resumed debt-equity swaps targeted for tourism projects.

Mexican leaders say they don't need to woo investors with bargains. They offer a newly opened market on the U.S. border, along with 85 million consumers and 27 million workers—many who earn \$4 a day. Mexico may be nowhere near ready

to sign a free-trade accord like that between the U.S. and Canada, but it's moving in that direction.

The thriving *maquiladoras* in the north make the border nearly porous for trade and for labor. Farther south, a little Silicon Valley has hatched in Guadalajara, 250 miles northwest of the capital, with Hewlett-Packard, Wang, IBM, and Unisys all assembling computers for export. Meanwhile, Mexican and American negotiators are hammering out a new bilateral auto pact, increasing prospects for a freer flow of

assembled cars and trucks.

Indeed, Mexico's border with the U.S. provides Salinas with two advantages over his Latin American neighbors. It makes the country a natural magnet for foreign investment. At the same time,

Washington's jitters about instability south of the border, while often a political headache for the Mexicans, give Salinas a trump card in negotiations with "the colossus of the north." The two contradictory notions combine to make the country a tough sell, even for a shrewd dealer like Salinas: He must frighten the U.S. into helping him, while assuring investors that all is well.

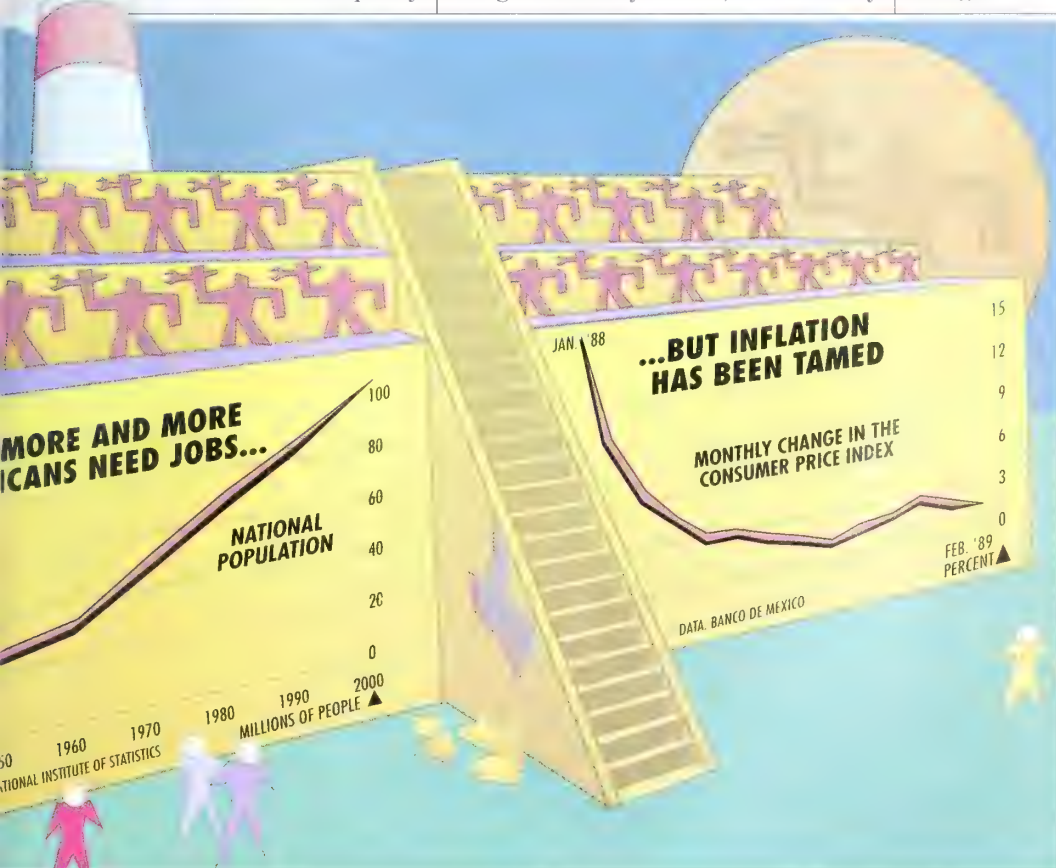
Neither scenario is sure. Mexico's only certainty is change. "Yesterday is gone," said the Spanish writer Francisco Quevedo, "but the morning has not yet arrived." In such times, events can sweep merely good presidents off course. To steer Mexico along his path, Salinas will have to be great.

By Stephen Baker and Elizabeth Weiner in Mexico City



HONDA'S GUADALAJARA PLANT: SALINAS IS WOOING JAPANESE INVESTMENT

vestors also hope to see a revival of debt-for-equity swaps, which give them a shot at discounted peso investments in return for reducing debt. The government shut down the popular scheme two years ago, citing inflationary effects, but in early



CHINA

CHINA'S ECONOMY IS CAREENING OUT OF CONTROL

As leadership falters, inflation and corruption are running amok

Ever since Deng Xiaoping launched China's economic revolution in 1978, the operating style for reform has been two steps forward, one step back. China-watchers have become so accustomed to these zigs and zags that few blinked last year when the government told the country to slow down.

But now the reform pace seems to be undergoing a decisive shift. On Mar. 20,

electricity, transport, and raw materials. Corruption is getting worse.

Short of fresh ideas, Li is reaching back to the 1950s for solutions. He wants to freeze prices, slow growth, and stifle dissent. Although economists applaud his moves, the odds against his succeeding are high. Regional leaders regularly and flagrantly disobey Beijing: They run their own pork-barrel construc-

China specialist at Princeton University

Beijing began trying to introduce retrenchment policies last September, but they have not worked well. A credit squeeze was supposed to curb inefficient rural factories and unneeded hotel projects. Instead, it is choking off much needed investment in transportation, energy, and raw materials. Price freezes increase costly subsidies, worsening the budget deficit.

Instead of suppressing demand by holding down wages, Li's policies have cut back supply, making shortages worse. Farmers, lacking fertilizer and suspicious after being paid in IOUs rather than cash last year, are refusing to plant this year's grain crop. Some 18,000 construction projects have been halted or delayed, swelling the ranks of the

unemployed. This is causing an enormous wave of illegal migration into prosperous provinces, especially Guangdong.

Some predict the shortages will choke off economic growth without stopping inflation—producing stagflation. This could mean getting stuck in Eastern European-style half-baked reforms, chilling China's transition to a market economy. Others say the economic reforms, now irreversible, will continue, but in a chaotic way.

Some foreign investors are feeling the pinch. A few projects are on hold, because the Chinese cannot come up with the needed construction funds. Others, planned as joint ventures, are going ahead as wholly for-

eign-owned investments because the Chinese partner cannot borrow any money to invest. Investors already operating in China encounter increased state interference, such as restrictions on necessary imports of parts.

GREATER UNREST? So far the cutbacks have not dampened the mood of potential investors from abroad. Some produce consumer goods that are still much in demand. Others are providing products, such as glass and cement, that are needed for construction, which is still booming in some regions. "Fortunately, nobody pays attention to Beijing anymore," says Owen Nee, a U.S. lawyer based in Hong Kong.

Many Western economists and diplo-



PRIVATE INDUSTRY IN WENZHOU: THE PROVINCES AREN'T HEEDING BEIJING

Premier Li Peng told 2,900 members of the National People's Congress to prepare for years of austerity. His speech made it clear that China is heading in a new, uncertain direction. The key question is whether Li or any national leader has the power to rein in an economy that is careening out of control (table).

When the Congress met last year, the mood was buoyant. Confident leaders allowed delegates to debate sensitive issues in public. This year the mood is somber and defensive. Critics were silenced in advance. And the absence of top leader Deng Xiaoping, 84, deepened worries about schisms at the top.

FIFTIES MENTALITY. Unlike past setbacks involving ideological disputes, the new retrenchment reflects fundamental economic problems. Prices last year rose 18.5% on average—more than 30% in the big cities. An 11.2% growth rate is clearly unsustainable because of shortages of

tion projects, sanction widespread corruption, and control the distribution of key commodities such as cotton and silk.

"No matter what bureaucratic solutions they try to impose, the local levels are well schooled in trying to get around these things, and they will," says one Western diplomat.

A failure by Li might convince Beijing that only market mechanisms can cure China of its economic ills. That full-speed-ahead approach was espoused by Party General Secretary Zhao Ziyang, but it was blamed for creating too many problems. Another possibility is that China could enter a prolonged period of confusion, with no clear direction from the center. "There's a tremendous dynamic in Chinese society [toward economic growth] that the leadership has very little control over," says David Bachman, a

CHINA OVERHEATS

	1987	1988
	Percent increase	
ECONOMIC GROWTH	9.4%	11.2%
FACTORY OUTPUT	16.5	17.6
RETAIL PRICES	7.3	18.5

SOURCE: CHINA'S STATE STATISTICAL BUREAU, BW

“What my little company needs
is the kind of computer only
a big company can afford.”



mats believe the quickest solution to China's tough economic problems is to reform rapidly and let the market cure all. But speedy reform, by exacerbating inflation, might cause unrest. Ironically, by postponing the tough decisions, China's leaders may be laying the groundwork for even greater unrest later.

All these problems would be challenge enough for Deng at the height of his

powers. But he is rumored to be seriously ill—and his failure to appear at the National People's Congress did nothing to squelch the scuttlebutt. One reason for the lack of unity and coherence in Beijing may stem from the fact that Deng's grip already is slipping. If that's true, China's voyage into uncharted waters may be a lengthy expedition.

By Dori Jones Yang in Hong Kong

JAPAN



SCHAL'S RUDISEL: THE COMPANY TEAMED WITH A LOCAL PARTNER TO WIN ITS FIRST JOB

U.S. CONTRACTORS FINALLY BREAK GROUND IN TOKYO

They're cracking open Japan's construction market—a project at a time

It looks like any construction site on Tokyo Bay: 12 acres of dirt, two dozen yellow bulldozers, and clusters of white-helmeted workers. But this \$138 million project for a conference hall and hotel for Yokohama has something unique: an American project manager. Just six months after receiving a Japanese construction license, Chicago's Schal Associates Inc. is digging in.

Schal's project signals the first major inroad by American companies into Japan's \$489 billion construction market. A joint venture with Japan's Toda Construction Co., the project comes nearly a year after Japan bowed to U.S. pressure and agreed to give American companies a crack at 14 public-works projects.

The Schal contract is a welcome step, but it doesn't end the U.S. construction industry's complaints about Japanese protectionism. Indeed, industry associations and politicians are pushing U.S.

Trade Representative Carla A. Hills to designate Japan an unfair trade partner after she completes her review of barriers to American exports on Apr. 30. U.S. companies picked up just \$7 million in construction contracts in Japan last year. In the \$403 billion U.S. market, Japanese companies grabbed contracts worth more than \$2.2 billion.

NO MARGIN. American complaints center on Japan's bidding system. U.S. companies argue that it's rigged to keep foreigners out of the market. But Japanese officials counter that only seven U.S. companies have applied for construction licenses. Says Hajime Sako, chairman of the Japan Federation of Construction Contractors: "We don't see much eagerness or effort by U.S. contractors to penetrate the Japanese market." The International Engineering & Construction Industries Council in Washington says more than 100 U.S. companies spent \$10

million last year trying to break into Japan.

The seven that won licenses heeded Japanese advice: They teamed up with top-ranked local partners. Schal, for example, has a 6% stake in its project with Toda. Although their winning bid was so low that neither company will turn a profit, Schal hopes to capitalize on being the first U.S. builder to win a Japanese public-sector project. Over the next 10 years, the government will spend an estimated \$15 billion to rebuild the Yokohama bay area. Says Schal's manager for Japan, Scott A. Rudisel: "We hope this will be a stepping stone to other projects in Japan and the rest of Asia."

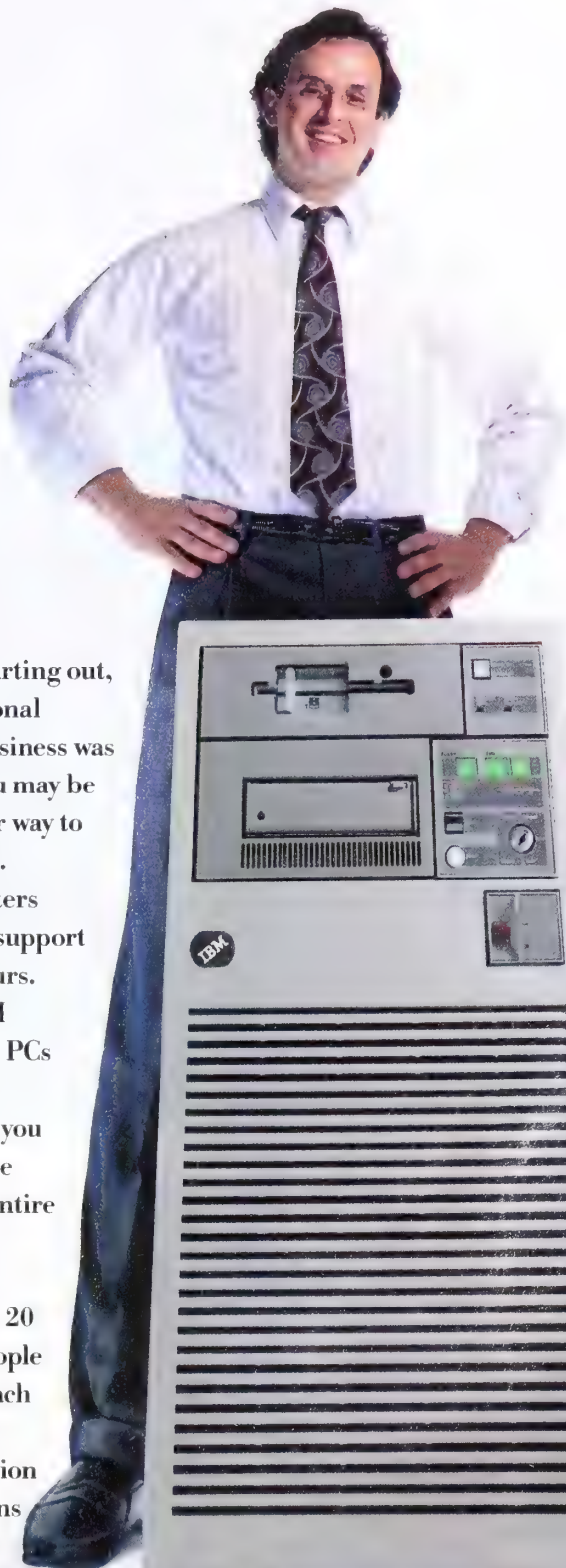
Other companies have since joined Japanese partners to bag private-sector contracts. Both Tishman Construction Corp. of Japan and Turner Construction Co. won jobs in March. Tishman's Tokyo unit inked a 50-50 deal with Aoki Corp. to build a \$200 million hotel in Osaka. Together with Kumagai Gumi Co., Turner is breaking ground on a \$77 million office building. Turner has a 10% share. Meanwhile, Overseas Bechtel Inc. grabbed a million-dollar research contract to build an artificial island near Kawasaki. "Bechtel has figured out how to play," says one ruling-party politician. "At this point, qualified Americans who come here will find a very warm welcome."

RIGGING CHARGES. Not all U.S. companies believe the welcome mat is out. Some still say they are hurt by Japan's *dango* system, under which companies bargain to decide who wins contracts. Under pressure from Washington, Japan's Fair Trade Commission charged a group of 140 contractors with rigging U.S. naval construction contracts worth \$155 million last December. But Senator Frank H. Murkowski (R-Alaska) claims that Japan's Construction Ministry barred the contractors from bidding for new contracts for only a month. "The Japanese government has been slow to prosecute offenders," Murkowski told a recent congressional hearing.

Despite the problems, the Japanese construction market may eventually reward shrewd and agile American players. In Tokyo alone, as much as \$32 billion will be pumped into redeveloping the waterfront over the next decade, Nomura Securities Co. estimates. For U.S. competitors, the next tests include a highway across Ise Bay and a new airport in Hiroshima. Continued pressure from Washington could open the door to a bigger U.S. stake in such projects. But companies will still have to work their way over the threshold.

By Naoaki Usui and Neil Gross in Tokyo, with Paul Magnusson in Washington

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CENTRAL AMERICA: BUSH MAY BE REDUCED TO A SUPPORTING PLAYER

The U.S. role in Central America, a major focus of President Reagan's foreign policy, seems destined to shrink under President Bush. That will leave to Central Americans more of the task of settling conflicts that triggered U.S. intervention in the first place. Although Bush is looking for new foreign-policy approaches and bipartisan solutions, he faces much the same impasse on Central America that Reagan encountered in Congress. If anything, Congress is likely to put new restrictions on U.S. actions in the region. And political developments in Central America are further narrowing the Bush Administration's room for fresh initiatives.

In El Salvador, a big victory in the Mar. 19 presidential election by Alfredo Cristiani, the millionaire candidate of the right-wing Nationalist Republican Alliance (Arena) made a shambles of the U.S. effort to build up the Christian Democratic Party of outgoing President José Napoleón Duarte. The Reagan Administration channeled aid to El Salvador, hoping that the Christian Democrats would provide a centrist bulwark against Arena on the right and Marxist guerrillas of the Farabundo Martí National Liberation Front (FMLN) on the left. But that effort was discredited by corruption among Duarte's followers.

The Bush Administration intends to continue aid to Cristiani's government, hoping that he will live up to the moderate tone he adopted in the election campaign. But Congress is wary of the power wielded in Arena by its founder, Roberto D'Aubuisson, who has been linked to death squads. Both houses of Congress are already moving to tie tight strings to Salvadoran aid. The House is expected to require Bush to certify that Cristiani is guaranteeing human rights and seeking a negotiated peace with the FMLN. But the guerrillas have stepped up their attacks, and the army is expected to react by demanding tighter curbs on political activity and civil rights. If Arena and the army become more repressive,

Duarte warns, "people could go off and join the FMLN."

For Nicaragua, Secretary of State James A. Baker III is shaping a policy that would keep the U.S.-backed *contra* fighting force intact as part of a new push for a peace settlement. Baker wants Congress to provide "humanitarian" aid to keep the *contras* in Honduran camps while he tries to enlist help from Canada and European allies to pressure Managua to adopt political reforms. The aim is to allow the *contras* to return to Nicaragua as civilians and compete fairly in elections next year. The U.S. would offer carrots, such as easing its trade embargo, while keeping in reserve a stick: the possibility of unleashing the *contras* militarily.

A VETO FOR PEACE? A big hitch is that Central America's five Presidents have launched their own plan for political liberalization in Nicaragua and for disbanding the *contras*. They intend to ask the U.N. Security Council to provide monitors to oversee the plan. That could force the Administration to make a politically tough decision on whether to veto the Central Americans' request.

On Capitol Hill, the most potent argument for *contra* aid is that lawmakers

who vote against it may be accused of abandoning Nicaragua to the Sandinistas. But even Baker's proposal for nonmilitary aid may encounter serious resistance, particularly among liberal Democrats who don't want to sidetrack the Central Americans' peace initiative. They suspect that if the U.S. plan hits snags, the Administration will eventually come back to ask for renewed military aid for the *contras*. What Bush faces is the same dilemma that produced a standoff between Reagan and Congress: Supporting the *contras* helps deflect hardline political pressures in the U.S., but there is widespread skepticism that the *contras* will help bring about a settlement in Nicaragua.

By Bill Javetski in Washington and Ana Arana in San Salvador, with Ruth Pearson at the U.N.



SALVADORAN CHILDREN AMONG RUINS

GLOBAL WRAPUP

SOUTH KOREA

To avoid stirring new uncertainties in a country beset by strikes and violence, President Roh Tae Woo on Mar. 20 postponed a referendum he had promised on his performance in office. Instead, he ordered a crackdown on leftist students and militants just as labor unions are launching their "spring offensive." But Roh faces continuing demands from opponents that he allow a full investigation of repression and corruption under Chun Doo Hwan, his predecessor and ally. Critics say Roh has been impeding the National Assembly's probe of Chun's rule.

To ease worries about his ties to

Chun, Roh had pledged during the 1987 presidential election campaign that he would give voters a chance to register a "midterm evaluation" of his presidency. He had been expected to announce such a vote soon. But many Koreans, like Roh, are worried about the unrest. It shows growing influence by leftist dissidents, observers say, among students, farmers, and workers. Some believe militants have been active in strikes by Seoul subway workers and at Hyundai Heavy Industries Co.

Reactions of Roh's foes to the postponement reflect their strategies for wearing him down politically. Kim Young Sam, runner-up in 1987's presidential election and leader of the sec-

ond-largest opposition party in the National Assembly, had hoped to benefit from the referendum. He expected the vote to repudiate Roh and force a new presidential election, which Kim expected to win. But Kim will accept the postponement, he says, if Chun testifies in the investigation of his rule.

Kim Dae Jung, who heads the Assembly's biggest opposition bloc, endorsed the postponement in hopes of winning Roh's backing, in return, for Kim's plan for provincial autonomy. It would give Kim's Peace & Democracy Party the chance to win control of many provincial and local councils and thus broaden his base for the next presidential election.

IS BILL REILLY TOO NICE TO RUN THE EPA?

The consensus builder faces tough turf and budget battles

It may be a kinder, gentler Administration, but Washington is still Washington. And during two months on the job, soft-spoken Environmental Protection Agency Administrator William K. Reilly has suffered culture shock.

In his 15 years at the helm of the Conservation Foundation, well known for its innovative solutions to environmental problems, he won a reputation for conciliation and mediation. Now, Reilly is finding that confrontation may have to become part of his repertoire. "He's a very nice guy whose success has been in finding the common ground," says John A. Moore, Reilly's No. 2 at the EPA. "Sometimes that's going to work, and sometimes he's going to have to be a hardball regulator."

Already, the Office of Management & Budget, which reviews actions of federal agencies, has held up Reilly's first moves as EPA head. On Mar. 10 the EPA issued long-awaited rules ordering the oil industry to reformulate gasoline to emit less vapor. Reilly also planned to roll out a proposal for more effective emission-control equipment on cars, a fight he was carrying on from his predecessor, Lee M. Thomas. But opposition from the OMB and the auto industry has put the plan on hold until the Transportation Dept. completes a safety review of the devices.

Also, EPA's budget has been held at a no-growth level for fiscal 1990. "Reilly's doing all the right things for a start," says Brent F. Blackwelder, vice-president of the Environmental Policy Institute, "but he's been placed under an incredible handicap."

PUSH FROM BUSH. Except for one very important thing. Unlike his predecessors, Reilly is getting support from the White House. On Feb. 8, Bush became the first President in the EPA's two-decade history to visit the agency's headquarters. Since then, Reilly has dined with Bush four times. The Bush Admin-

istration will "take the environmental high ground," Reilly promises. "We will make progress."

Even with his EPA office still undecorated, Reilly is rolling up his sleeves for action. A thoroughgoing Ivy Leaguer—Yale College, Harvard law school, and a graduate degree in urban planning from Columbia—he is getting used to the idea of spending less weekend time with his

Some Washington insiders believe Reilly may even be able to smooth over relations with the OMB. Robert E. Grady, the OMB's new point man on the environment, has considerable political acumen and may want to burnish Bush's image as an environmentalist. The Bush OMB, Grady declares, is "more in tune with what Reilly's trying to accomplish than past OMB staffs might have been."

'POINT OF CORRECTION.' Already, Reilly and Grady, along with White House Counsel C. Boyden Gray, have visited Capitol Hill to confer on clean air. Bush's plans for amending the Clean Air Act, which he hopes will break an eight-year deadlock, are expected to be released in May. Reilly will soon begin to make changes in the highly criticized Superfund dumpsite cleanup program.

Reilly's negotiating ability is already serving him well in dealing with global



REILLY'S CHALLENGES

AIR QUALITY Disputes in Congress have blocked reauthorization of the Clean Air Act for the past eight years

HAZARDOUS WASTE The \$8.5 billion Superfund program is dragging. Only 40 dumps have been cleaned up

GLOBAL POLLUTION International efforts are needed to deal with the greenhouse effect and the ozone layer

GARBAGE GLUT Americans produce more refuse per capita than any other nation. Landfills are nearing capacity

DATA: BW

family at their 33-acre Virginia farm.

It is Reilly's ability to forge a consensus between opposing groups that has won him respect from industry and environmentalists alike. At the Conservation Foundation, he was able to hammer out tough positions on groundwater and wetlands protection.

In the face of criticism from some environmental activists, Reilly insisted that an effective tactic in getting hazardous waste sites cleaned up was to avoid lengthy litigation. So he helped found Clean Sites Inc., a group dedicated to helping companies work out joint settlements for cleanup of Superfund sites. "Reilly was the glue that held all this together," says H. E. McBrayer, president of Exxon Chemical Co.

environmental issues. He was instrumental in getting U.S. support for an international ban by the year 2000 on chlorofluorocarbons, which destroy the ozone layer. Reilly, who speaks French and Spanish, is adding an assistant administrator for international affairs.

The U.S., Reilly says, is at a "point of correction," requiring a new environmental policy to make further progress without compromising economic growth. To his former colleagues, that seems a tall order, and skeptics abound. "We'll look at what they do," says Daniel Weiss, a Sierra Club director, "and not at what they say." That might mean the smooth mediator will have to become a bit of a streetfighter.

By Vicky Cahan in Washington

The book that butchers Corporate America.

These ten sacred cows represent the conventional business wisdom.

Bottom-Up Marketing, the new book by Ries and Trout, advocates the opposite, or what might be called the "blasphemy."

A blasphemy is not necessarily wrong. It just might be a little ahead of its time.

As George Bernard Shaw once said, "All great truths begin as blasphemies."

1. Mission statements.

The wisdom. A mission statement helps define what a company wants to be when it grows up.

The blasphemy. Forget about "what you want to be." Focus all of your efforts on "what you can be."

2. Long-term planning.

The wisdom. Long-term planning is critical if a company is going to fulfill its mission.

The blasphemy. A long-term strategic plan is useless unless you are doing your competitors' plans as well.

Long-term planning didn't make Xerox a factor in office automation and didn't keep GM from losing 13 points of the automotive market in the past decade.

3. Goals.

The wisdom. A company needs market share and return-on-equity goals to work towards.

The blasphemy. Goals are of little use in marketing. The trick is to isolate the problem, face it squarely, then go all-out.

4. Decentralization.

The wisdom. Decentralization is good. It gets you closer to the market.

The blasphemy. Decentralization is bad. It dissipates your force and makes it difficult to keep things focused.

Just being closer to the market is no advantage if you are not organized to make a bold move.

5. Line extension.

The wisdom. Extending the equity of a brand (also known as line extension) makes a lot of sense. It saves money.

The blasphemy. Line extension makes sense only if specialized competition can be kept out of the marketplace. But this rarely happens because you can't control what your competitors do.

6. Serving the customer.

The wisdom. "Serving the customer" is the name of the game. It's just us and our customer.

The blasphemy. This is fantasy. There are no virgin markets. Marketing is taking customers away from your competitors while you hold onto your own.

7. Trying harder.

The wisdom. To win, all you need is a better effort. Better sales training, better pricing, better advertising, to name a few of the more popular "betters."

The blasphemy. Trying harder is not the secret of success. Often the best answer to a problem is trying "something else."

the ten sacred cows of

8. Success takes time.

The wisdom. Success takes time to develop. Don't expect instant results.

Managers often justify short-term losses with predictions of a glowing future...always three to five years away.

The blasphemy. Early losses are usually followed by even greater losses. Big successes are usually successful from day one.

9. Marketing is complicated.

The wisdom. Marketing is really a complicated function involving the coordination of many disciplines.

The blasphemy. Marketing is simple. It's a battle of oversimplified ideas in the mind of the prospect.

When you perceive marketing as a complex function, you rob yourself of the ability to see the simple solution, the only solution that has a chance of working.

10. The big picture.

The wisdom. Top managers should not get immersed in details. They should be free to think long-term.

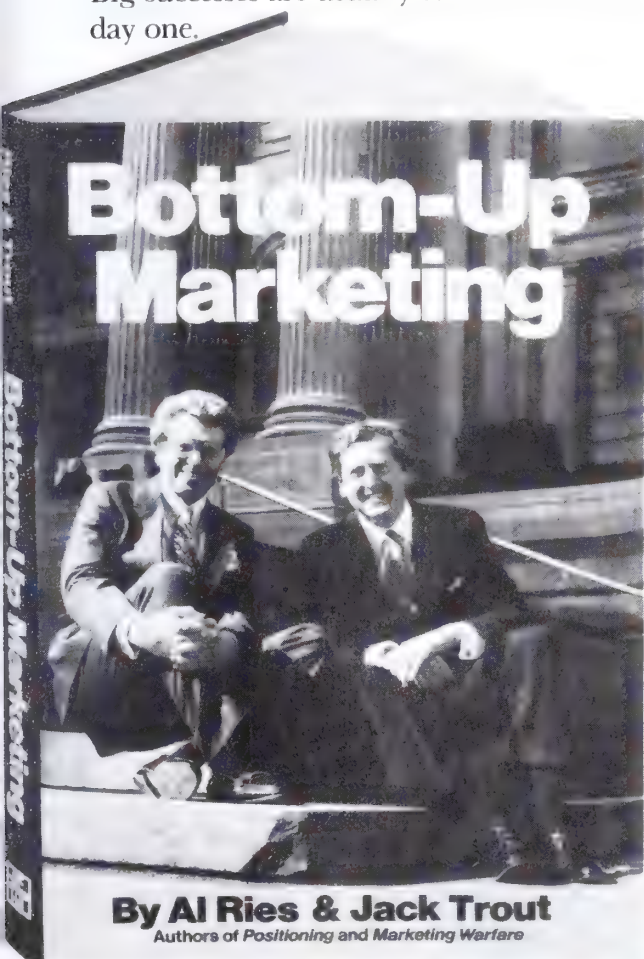
The blasphemy. Corporate chieftains should get down in the mud of the marketplace. That's where they'll find the tactic they can turn into a strategy.

This is the essence of the bottom-up approach to marketing.

How to order the book.

You can buy *Bottom-Up Marketing* and an audiocassette featuring Al Ries and Jack Trout at most fine bookstores.

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U.S. COMPANIES GO FOR THE GRAY

They're planning a major marketing shift as baby boomers age

American Telephone & Telegraph Co. is learning how to reach out and touch some older customers. The company hires retirees, briefs them on AT&T products, teaches them how to give presentations, and sends them on the road to win over other consumers their age. The result? AT&T credits the salespeople with helping it keep older customers from switching to competitive long-distance services. And managers are learning a few things about the elusive 50-plus market. "They want plenty of information about products," says Sheila Spencer, national manager for the mature market. "And they don't want you to beat around the bush."

AT&T is confronting one of the biggest challenges in marketing since the end of World War II: the aging of America. The full impact won't be felt for several years, when the first baby boomers start hitting 50, but smart companies are changing the way they do business now. That's because people over 50 already control 75% of the nation's wealth and half the discretionary income. In ways

both subtle and obvious, this age wave is rapidly transforming everything from product development and design to marketing and advertising.

Today's 50-plus consumers aren't behaving like their parents and grandparents. They're wealthier, healthier, and better educated. This presents lavish opportunities for marketers. But inadequate planning can also create major risks: Executives are often amazed to find out how fast their mainstream customers are aging, and some companies first encounter the senior market when they begin receiving complaints from older customers.

Even companies that have long catered to an older clientele have to work hard to keep their franchises. On the cruise ship *Crown Odyssey*, for example, passengers take water-aerobics classes, order broiled fish with lemon, and attend seminars on stress reduction. Sounds like a shipful of health-conscious yuppies, right? Wrong. Royal Cruise Line, the San Francisco-based operator of the *Crown Odyssey*, is simply trying to



please its customers, most of whom are 55 and older. "Passengers are probably more active mentally and physically a 60 than even they thought they would be," says Executive Vice-President Duncan Beardsley.

As Royal's efforts show, these people don't fit the stereotype of sickly, set-in-their-ways, tight-fisted old folks that has dominated marketing images in the past. And companies that have learned to sell to this generation of 50-plus consumers will have a big headstart when the first baby boomer turns 50 a scant eight years from now. For decades, the baby boom's demography has been destiny for much of American society and business. As this population bulge moved through its teens, twenties, and thirties, it influenced politics, shaped media, and determined the rise and fall of whole industries. Now these affluent boomers are growing older—and the U.S. will increasingly become a senior society.

NEW PITCHES. That means almost all marketers will have to reject their conventional wisdom of targeting 18-to-49-year-olds and find new ways to appeal to the aging consumers who will make up the bulk of U.S. buying power. "There is no reason to believe the entire baby-boom generation will stop consuming once they turn 50," says Penelope Queen, planning and marketing director at Saatchi & Saatchi Advertising.

THE FOUND GENERATION American Express and General Foods count on peer appeal



RETIRING TYPES

To reach them, companies are backing special events and promotions. Copper Mountain Resort has a club for older skiers; AT&T offers special products and services. The U. S. National Senior Olympics is sponsored by mass-marketers



General Motors Corp.'s Cadillac Motor Div. is struggling to prepare for that day. Cadillac's average buyer is 47, and the company has long been considered a veteran at attracting older drivers. But it is already having trouble keeping customers: Cadillac's market share has dropped significantly since 1983, and its appeal could shrivel even more among aging baby boomers, who grew up buying imports. To lure them, Cadillac has introduced European styling in a limited edition of its Seville model, which features leather seats, air suspension, and a clean, no-chrome look. Foreign competitors as well are trying to keep their aging car buyers. Honda Motor Corp., for example, used a 50-over-50 couple in one of its ads for the first time this year. Instead of the usual pitches for speed and performance, the commercial stressed room and comfort.

A broad range of products and industries stands to gain as America ages. Take health care. The medical rehabilitation market alone, now an estimated \$11 billion business, is expected to exceed \$15 billion in three years. People over 50 already account for more than 60% of all leisure travel, according to the American Association of Retired Persons (AARP). That number will only increase as more people retire. Financial services companies such as Travelers

Corp. and American Express Co. are offering special financial-planning services for retirees. Home exercise equipment, retirement housing, and cosmetic industries will all get a boost from the 50-plus explosion.

But buying patterns are also shifting in unpredictable ways. When Sharp Electronics Corp. introduced its Half-Pint microwave oven, for example, it figured

the product would appeal to young singles too busy to cook. Actually, more than a third of all Half-Pint buyers are people over 65 who no longer cook big family meals, says Anne Howard, Sharp's national marketing manager for appliances. Makers of musical instruments have found a growing audience in retirees who may have studied music as children but only now have the time to take it up again. A particular favorite: the electronic keyboard, which can be played using earphones so no one else can hear.

ENGINEERING EDGE. Increasingly, companies realize that new products and services need to be developed with the aging consumer in mind. Beecham Products USA, maker of Geritol, is developing new skin-care products for its Calgon line of bath products to help pamper older skin. AT&T's phone-receiver amplifiers, automatic emergency dialing attachments, and daytime long-distance discounts cater to retired customers.

Similarly, plumbing and fixture maker Kohler Co. makes shower stalls with grab bars, wheelchair-friendly sinks, and higher toilets that don't look institutional. Such catalogs as *Comfortably Yours* offer nonslip bathmats and dishes that can be filled with hot water to keep food warm longer. General Motors engineers are experimenting with bigger buttons, simpler operating instructions, and larger doors on cars such as Oldsmobiles.

Retailers, too, are looking at improving their store design and merchandising mix to attract older consumers. Several supermarket chains have installed benches and restrooms in some of their

stores. Recognizing that body shapes change as people grow older, The Limited Inc. is expanding its Lane Bryant large-size women's apparel chain. Dress Barn Inc. in Stamford, Conn., has started a new store carrying large sizes. Even Perry Ellis and Ralph Lauren are producing larger designs.

The aging of American consumers is changing not just the products and services aimed specifically at seniors but many mass-market products as well. Sharp discovered that older buyers found touch-control microwaves unnecessarily complicated. So the company came up with preprogrammed keys for the most common dishes.

HOW COMPANIES ARE COURTING OLDER CONSUMERS

AT&T Sponsors retirement fairs and festivals aimed at seniors; offers emergency dialing attachments, amplifiers, and daytime long-distance discounts

SHARP ELECTRONICS Developing a VCR that talks viewers through the programming steps; is working on simplified instructions for computers

GENERAL FOODS Uses older celebrities such as Lena Horne and Rue McClanahan in ads for Post Bran Flakes; shows cheerful older people in Jell-O ads

TRAVELERS Offers special 50-plus financial advisory services to help clients plan for retirement

BEECHAM PRODUCTS USA Shows younger people in new ads for Geritol; offers Somnifex sleep aid in easy-to-swallow liquid form; uses large type on product labels and easy-to-open packages

DATA SW

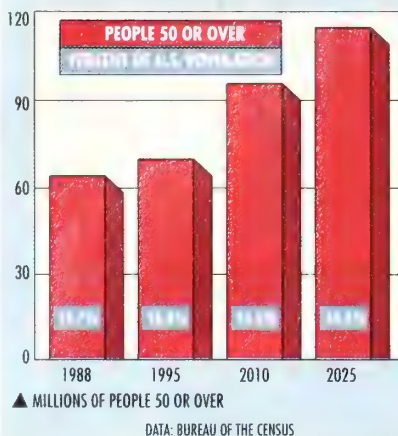
such as baked potatoes or frozen meals. Beecham has begun using easier-to-read type on its labels and instruction pamphlets. And Whirlpool Corp. replaced the hard-to-read operating instructions on washing-machine lids with high-contrast, oversize graphics. The company also added bigger, softer knobs.

To reach older consumers, many mass-market companies are sponsoring special events and promotions. General Foods, Digital Equipment, Holiday Inns, and Trans World Airlines all back the U.S. National Senior Olympics, for example.

TUNNEL VISION. Such innovation and flexibility is still more the exception than the rule, however. So far, most companies are doing little to prepare for the demographic switch. More than 40% of the nation's leading advertisers said the 50-plus market has little impact on their current marketing strategies, according to a survey by Vitt Media International Inc. "Almost every study we do deals with consumers 18 to 49," adds Judith Langer, head of Langer Associates Inc., a New York-based market research firm. "I want to ask, 'What about older people?' But I know it's a lost cause."

If marketers are slow to understand

THE AGING OF AMERICA



the mature consumer, blame it on years of practice. "In our culture, we value young people and think of them as the future. That automatically denigrates older people," says Ken Dychtwald, head of Age Wave Inc., a research company in Emeryville, Calif. Seniors have long been considered an undesirable consumer market. And not too long ago there was some basis to that belief. As recently as the late 1950s,

one-third of the nation's elderly were impoverished. Even those who had money were slow to spend because their attitudes were shaped by the Great Depression.

But yesterday's wisdom doesn't apply to the growing 50-plus population. By the year 2000, 21% of seniors will have household incomes in constant dollars of more than \$50,000, up from 12% in 1985. By 2005, 40% of people older than 50 will have a college degree, up from less than 25% now. Thanks to medical advances and healthier lifestyles, older consumers will be more active than ever before. And studies show that they will try new products and change brands often, if manufacturers give them a reason to switch.

'FOR OLD HAIR.' But there are pitfalls in courting this growing market. Companies must be careful that they don't just slap a new label on an existing product and figure they've got the 50-plus crowd snagged. When Gerber Products Co. introduced Singles, a line of pureed foods for adults, it seemed like a natural for denture wearers. But the product never took off, partly because older consumers were embarrassed to buy meals that came in baby food jars.

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Documents created using Wordperfect 5.0 and Harvard Graphics

Johnson & Johnson Inc. made a similar mistake. The company first marketed its Affinity shampoo as the shampoo for old hair—and who wants old hair? When sales went nowhere, J&J repositioned the product for a more general audience. Kellogg Co. may be falling into the same trap with its 40-Plus Bran Flakes. It put the new name on an existing cereal when it discovered that more than 60% of bran-flake buyers were over 45. "You can't target age so blatantly," says Langer. "I doubt people over 40 need a special cereal."

Mistakes in the mature market can be costly. This new breed of consumers will not be pushed around. One-third of older Americans have boycotted products and services because of inappropriate age stereotyping, according to a Georgia State University study. "Many marketers seem to be replacing tired old misconceptions with bright new distortions," says James M. Thompson, AARP's manager of consumer affairs.

AARP, with 30 million members, has become one of the most powerful lobbying groups in the country. It is also a strong marketing force. Members can buy health, auto, and homeowner's insurance and get discounts on air travel, motels, rental cars, prescription drugs, and health aids. AARP's 19.4-million circu-

SENIORS: BIG SPENDERS

People over 50 account for about 26% of the U.S. population, but their share of spending in key areas is far higher.

	Purchases by consumers over 50
LEISURE TRAVEL	80%
DOMESTIC CARS	50
SILVERWARE	50
HOME REMODELING	44
COSMETICS AND BATH PRODUCTS	37
LAWN AND GARDEN PRODUCTS	33

DATA: AMERICAN ASSOCIATION OF RETIRED PERSONS, BW

lation *Modern Maturity* magazine, reflecting readers' wishes, won't take advertising that puts older people in a negative light or focuses on pain and suffering.

BRIGHTER IMAGE. While plenty of companies have offended the 50-plus market, advertisers more often simply ignore it. "You only see 35-year-olds and 75-year-olds on TV," says Barbara S. Feigin, executive vice-president of strategic services at Grey Advertising Inc. "It's as if people in their fifties are a lost generation."

And a lost opportunity. People in this market respond well to advertisers

who show older people in happy, productive, and fun settings. Sales of General Foods Corp.'s Post Natural Bran flakes have gone up 10% since GF began using ads with Lena Horne, Rue McClanahan of *Golden Girls*, and Steve Allen. Research also shows that older viewers like Coke Classic ads featuring Art Carney with a young boy who plays his grandson.

Discounts and promotions that play down age but play up value are also effective. About 60% of 50-plus consumers use senior-citizen discounts at least occasionally, according to market research firm Yankelovich Clancy Shulman. Waldenbooks Inc. and Sears, Roebuck & Co. have been successful with special deals for people over 50. Some 300 skiers joined the "Over the Hill Gang" this winter at Copper Mountain, a Colorado ski area that offers discounts and activities for skiers over 50.

"Discounts are nice, but they don't go the distance," warns Dychtwald. "Companies need to sit down and determine exactly what strategies they are going to use to capture this consumer." Marketers that don't heed that advice may be overlooking America's most influential group of spenders.

By Walecia Konrad in New York and Gail DeGeorge in Miami, with bureau reports

But they keep looking at the evidence.

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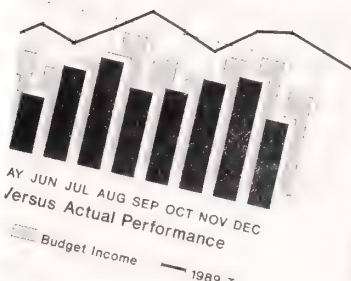
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 **HEWLETT
PACKARD**



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So it's not surprising that BMW's 5-Series is the family-size four-door that "effectively recalibrates the performance sedan benchmark"

deemed the new standard in its class. And it reassures the mind with superior anti-lock disc brakes and a unitized steel body that is

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The experience is yours by contacting your BMW dealer and test driving the 5-Series sedan.

The car you need, reconciled with the car that you really want.

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INFORMATION MANAGEMENT

USING THE LAW TO REIN IN COMPUTER RUNAWAYS

More unhappy buyers are taking systems suppliers to court

For Geophysical Systems Corp., it was a spectacular takeoff and crash. In 1981, just three years after it invented a device that for the first time used sonar to determine the production potential of oil and gas discoveries, the Pasadena (Calif.) company earned \$6 million on sales of \$40 million. Two years later it was hiding from creditors in Chapter 11. Geophysical's misadventure was that it hired a Raytheon Corp. subsidiary, Seismograph Service Corp., to build a \$20 million computer system that would process the sonar-generated data. The system couldn't do it. And Geophysical's clients, a virtual who's who of oil and gas, canceled their contracts.

In 1985, Geophysical sued Seismograph. Finally, last December a Los Angeles jury awarded Geophysical \$48.3 million to cover computer-system costs and lost profits, although the judge in that case has ordered a new trial to review the size of those damages. Geophysical had claimed that the Seismograph system couldn't meet its complex computation requirements—and that Seismograph knew this before it started building the system. By finding for his client, says

Robert Badal, Geophysical's attorney, "the court is saying that if we wanted a computer unable to handle our data we could have gone to Toys 'R' Us and been out \$20 instead of \$20 million." Seismograph contends that the system worked and that Geophysical's sales decline was caused by falling oil prices. It has appealed.

The Geophysical case highlights a new battleground between computer purchasers and suppliers. As computer runaways—systems that are over budget, installed late, or don't work—become endemic, fed-up customers are fighting back. And they're using the law to do it. In 1988 the American Arbitration Assn. took on 190 computer disputes, most of

them concerning defective systems, totaling \$198 million in claims. That was up from 123 cases in 1984, representing claims of \$31 million.

Dozens of law firms now specialize in high-tech matters. Typical is Atlanta's Morris, Manning & Martin, which so far this year is seeking \$15 million in damages for computer runaway clients, vs. about \$1 million five years ago. What's more, the Computer Law Assn., a group of attorneys that concentrates on high-tech legal cases, has grown from eight members 18 years ago to more than 1,200 today.

OUT OF KILTER. The Geophysical award stands out because it's so hefty. More typical of runaway litigation is the case involving a division of Pittsburgh-based Joy Technologies Inc. and computer supplier Qantel Business Systems in Hayward, Calif. In 1984, Joy hired Qantel to install a \$250,000 computer system to track Joy's billings for hydraulic landing gear that it sold to the Pentagon. From day one, according to Joy, the system failed to keep the books adequately, and soon Defense Dept. payments were months behind. Joy claimed that its cash flow suffered.

So in 1986, it sued Qantel for \$2 million to recover the cost of the original system, the cost to replace it, and loss of income. Qantel argued that Joy exaggerated its losses and that the computer system worked. But a federal judge refused to throw out the case during pretrial motions. And soon afterward, Qantel settled for \$500,000 without admitting liability. Joy was elated. "Two years is an extraordinarily short time to

THINGS TO DEMAND WHEN BUYING A COMPUTER SYSTEM

- ▶ **ACCEPTANCE TEST** Requires the supplier to run the customer's actual data successfully through the system
- ▶ **GUARANTEE** The customer pays leasing or purchase charges only after the new system has been working correctly for two months
- ▶ **BINDING ARBITRATION** Stipulates that the customer can elect to have disputes resolved by an outside arbitrator
- ▶ **SOFTWARE OWNERSHIP** Gives the customer the rights to the system's source code and leaves it in the customer's possession
- ▶ **SUPPORT** Guarantees that support and servicing for the system will be available for at least a year—even if the supplier goes out of business

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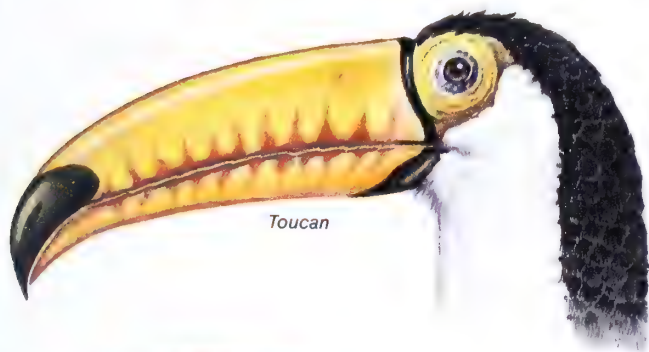
Crimson-backed
Woodpecker



Golden Eagle



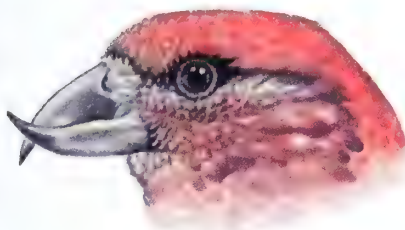
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get a settlement covering twice the amount of cash paid," says its attorney, Richard Raysman.

While such successes sound impressive, litigation isn't for everyone. When a customer sues, it loses its computer supplier. It may take years to find a replacement and build a new system—not to mention win the original suit. Because of this, says Hank Jones, an attorney at Morris Manning, "when you sign a contract for a computer system, you're locked in a deadly embrace with the supplier that you may not be able to, or want to, get out of."

IN A BIND. Frequently, what cements the embrace is the contract for the system. The boilerplate agreement that suppliers traditionally offer includes numerous so-called exclusions of warranty that limit the supplier's liability for system

"We told them we didn't want to blackmail them or hurt their reputation. We just demanded something that worked"

failures or delays. Also, the contract usually states that nothing in it is binding unless specifically spelled out. That, says New York attorney Fred Rubinstein, means that "not everything in the wonderful sales pitch is included in the vendor's commitment." Frank Remkiewicz, a former senior consultant at Price Waterhouse, recalls telling customers that it will take "only 72 hours for a crucial software project. But we wouldn't put this into the contract. Then when it took us two months to do the job, we simply explained that the project now costs more because the extra work we did was out of the scope of our agreement." Price Waterhouse won't comment on this.

For customers whose contract favors the supplier, the only way to slow down a computer runaway is a tortuous negotiation during which every bit of leverage is put to work. This just happened to the State of New Jersey, which in 1983 hired Price Waterhouse to build a \$6.5 million system to handle licensing and traffic violations records for the Motor Vehicles Dept. The system was installed on time two years later. But it didn't have enough capacity, and paperwork for thousands of licenses and traffic summonses was mailed late or lost.

The state was in a bind. In its contract, the Big Eight firm's liability was limited to a maximum of \$500,000 in damages. Generally, computer suppliers

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demand a stipulation of this sort when dealing with governments to avoid huge citizen class actions. What's more, New Jersey needed a working Motor Vehicles Dept. immediately and couldn't afford years of chaos during litigation. "We told them that we didn't want to black-mail them or to hurt their reputation. We just demanded that we get something that worked without spending millions more in taxpayer dollars," says Donald R. Belsole, first assistant attorney general of New Jersey.

Price Waterhouse agreed—especially because this computer runaway was generating negative publicity. So while the attorneys haggled over a settlement during nearly two years of negotiations, the accounting firm fixed the system. Finally, an agreement was reached last December in which New Jersey got the system for \$1.2 million less than the contracted price. And Price Waterhouse swallowed approximately \$2 million in additional project costs.

TILTING SCALES. New Jersey was in a unique position in this case: It has millions of dollars in potential future contracts that Price Waterhouse wanted a chance to bid on. But for most other computer buyers, the best protection is to revamp the supplier's contract before signing it. For instance, many customers are starting to demand a clause providing for binding arbitration of disputes, which usually is concluded in just 6 to 10 months. To be effective, attorneys say, this clause should spell out such details as the number of arbitrators, their backgrounds, and the location of the arbitration hearings to avoid hometown bias. Another contract provision that many customers require is the so-called acceptance test. It obligates the supplier to successfully run the customer's real data—sometimes hundreds of forms—through the computer before the customer pays.

Surprisingly, the new legal aggressiveness of customers isn't particularly troubling to most systems suppliers. They say it's the natural tilting of the scales as the supply of practitioners in the \$8 billion systems-consulting market outstrips the demand for services. Considering that, says R. W. Davis, McDonnell Douglas Corp.'s director of systems integration, "it's appropriate now that customers make sure they're getting what they think they're buying." Other suppliers add that customer activism may even reduce the number of run-aways from an estimated 35% of all current computer projects. Says a systems designer at one Big Eight firm: "It could be just the thing we need to make us more honest."

By Jeffrey Rothfeder in New York

BusinessWeek Travel Facts

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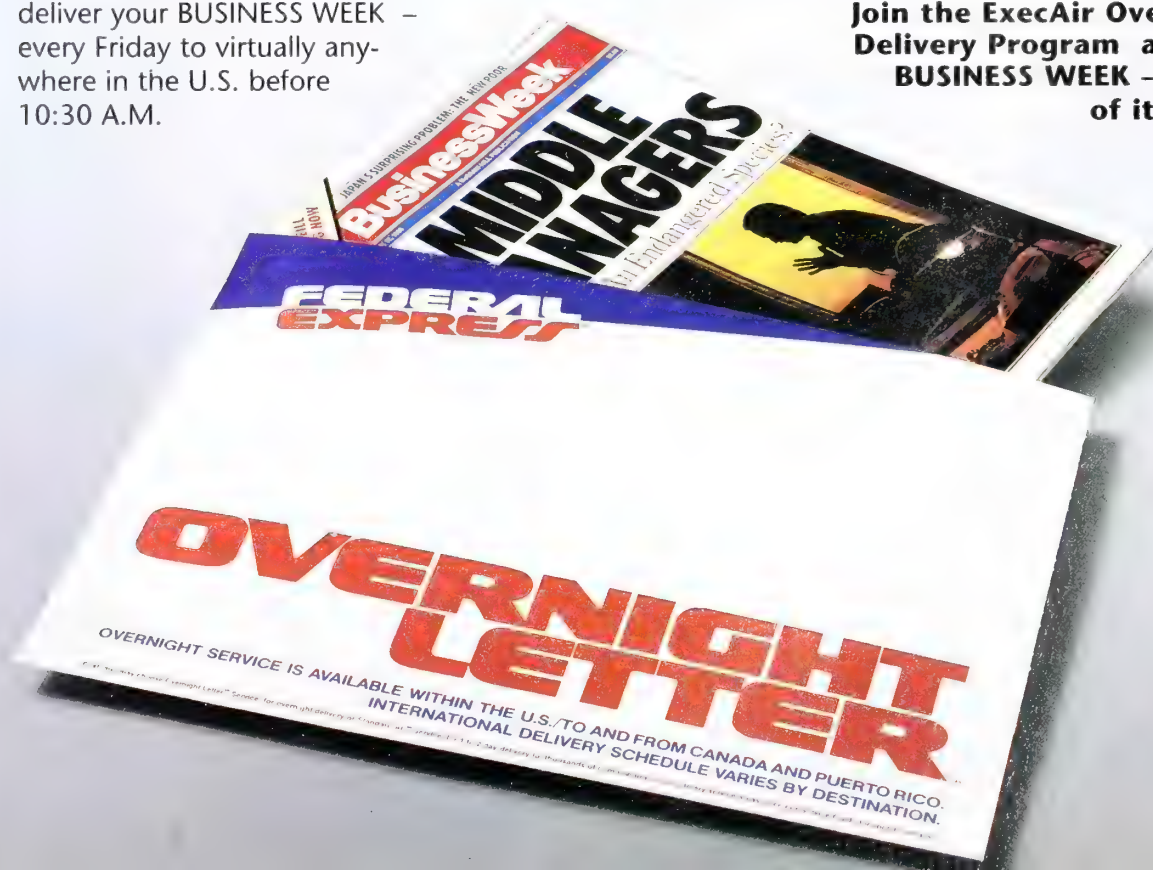
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DU PONT'S VERSION OF A MAVERICK

When Edgar Woolard becomes CEO, the slow-moving giant may have a catalyst for change



Ask Edgar Smith Woolard Jr. to name his worst flaw, and he draws: "Impatience." In 1969 it almost derailed his career. Facing a long climb up the Du Pont Co. ladder, he left for a top job at a textile maker near home in tiny Washington, N. C. Soon regretting his choice, Woolard talked a sympathetic boss into taking him back. And he got some free advice: He'd have a good future at Du Pont if he'd just "serve his time."

Woolard apparently learned to stifle his impatience. On Apr. 26, the 55-year-old Du Pontier will be named chairman and chief executive of the \$33 billion company. For the past six years he has been a CEO-in-training as a member of Du Pont's Executive Committee—the seven top corporate policymakers.

ATTITUDE ADJUSTMENT. As part of the inner circle, Woolard readily accepts his share of the blame for Du Pont's lackluster performance in the past several years. While less diversified rivals such as Dow Chemical Co. and Rhône-Poulenc have enjoyed an earnings surge since early 1987, Du Pont has lagged behind because of costly moves into oil, electronics, and pharmaceuticals (chart). Its

sales last year rose 8%, but pretax income increased just 4.5%, to \$3.8 billion. And that was largely from cyclical gains in its mainstay polymers, textile fibers, and chemicals units.

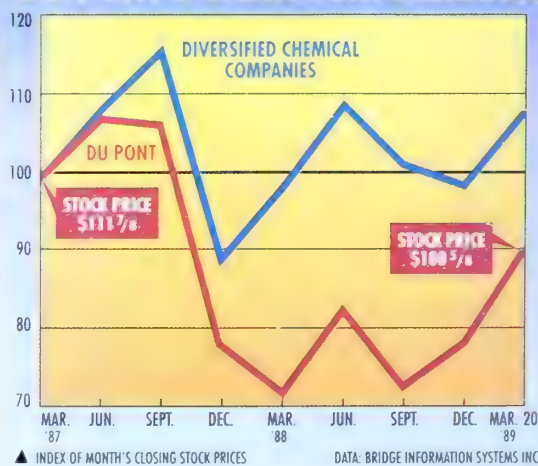
But there is change afoot. Along with a dividend hike, the company recently announced that it would repurchase 20 million shares, or 8% of its outstanding common. That may not seem like much to crow about, but it's Du Pont's first major buyback ever. Shareholders perceive a change in attitude at the company, and as a result, its stock has climbed to about 100 from the low 80s just three months ago. What's more, they think Woolard is open to more buybacks, dividend increases, and perhaps jettisoning some operations.

Wishful thinking? Perhaps. Woolard, after all, assures everyone: "It's not like someone is handing me the ball to run off in a new direction." But in his low-key way, he has made

it clear he thinks shareholders should expect more. Woolard's rise to CEO was backed by the company's biggest stockholder—Montreal's Bronfman family. The Bronfmans control a 23% stake in Du Pont and 6 of 24 board seats. They see Woolard as a hard-nosed manager who will boost results and the stock price, says a source close to the family.

But the bureaucratic process at Du Pont looms large. If Woolard pushes for

DU PONT'S WEAK PERFORMANCE



any strategic retrenchments, he would have to persuade two former chairmen who still sit on the board that their handiwork was, perhaps, misguided. That's a tough job, considering that departing Chairman Richard E. Heckert describes the company's style as "evolutionary, not revolutionary." And Heckert, who often spars with Woolard on policy, will head the board's powerful finance committee for five years.

Heckert's predecessor, Edward G. Jefferson, will serve on the board for three more years. It was on his watch that Du Pont began diversifying in earnest. He snapped up Conoco Inc. for \$7.8 billion in 1981. Not only did oil prices take an immediate dive, but investors have never quite forgiven management for raising half of the purchase price by floating 79 million new shares. Conoco accounts for 30% of Du Pont's sales and just 16% of operating profits. Since 70% of Du Pont's products are hydrocarbon-based, Woolard insists he will not sell Conoco wholesale. But analysts aren't ruling out some oil and gas asset sales, or a partial spinoff to the public, to boost the stock price.

Woolard supported and vows to continue Du Pont's push into electronics and pharmaceuticals, businesses that could make up the slack when growth of its mainstay products slows in the 1990s. The \$1.8 billion electronics unit has a nice position in films and imaging, and sales are growing at a 15% pace. But it has plowed hundreds of millions of dollars into such areas as fiber optics and optical disks—where competition is voracious and a payoff is years away.

SLOW DELIVERY. The pharmaceutical unit has been a money-loser. Since 1982 the company has spent more than \$1.7 billion in capital and research costs. While Woolard is pressing for faster drug development, only one of Du Pont's 23 drugs in the pipeline, an anti-arrhythmic heart medication, has hit the early stages of a Food & Drug Administration review. Others could be a decade off. Says Stuart Wamsley, executive director of Morgan Stanley International: "They should just chuck the thing and sell it off to somebody else."

Investors don't really expect much soon from these diversifications. If they are right, Woolard will have to resort to other means to make earnings grow. He has already demonstrated his ability to wield a knife. He cut jobs by 20% to restore profitability when the textile fibers segment ran aground in the late 1970s. Now the \$5.8 billion department is Du Pont's second-biggest sales generator and top moneymaker. Clearly, Du Pont management has become less forgiving: One of every five jobs that existed in the early '80s has been eliminated. And there is pressure for more cuts.

Woolard must bring his marketing instincts to bear as well. He blessed the decision years ago to advertise Du Pont fibers directly to the public, a costly move that eventually resulted in soaring sales of Stainmaster carpet. Now, Du Pont sorely needs to hit on new marketing approaches and show more sensitivity to customer demands in other lines. Take its automotive materials division. Car designers give rivals higher marks for solving materials problems, though they think Du Pont is getting better. Just a year ago, Ford Motor Co. was having trouble with the mirror housings on its cars. Paint was chipping off the Du Pont plastic. General Electric Co. came up with a better material—and stole the business. Du Pont says it likewise has taken business from GE.

Another challenge: Woolard wants

Du Pont's \$1.4 billion research and development budget to be managed more efficiently. He has only to point to Kevlar, the bullet-resistant fiber that cost \$600 million to develop and market, a sum that top executives say Du Pont will never recoup. Or to Qiana, a synthetic silk that cost \$260 million before fashion changes forced Du Pont to drop it.

Du Pont shareholders may think that Woolard is their man. But they've been fooled before. When Jefferson engineered an unprecedented round of early retirements back in 1985, Wall Street was sure a new era of investor consciousness had dawned. But as always, change occurs slowly at Du Pont. This time, investors are hoping that Woolard hasn't rid himself of his professed worst flaw: impatience.

By Joseph Weber in Wilmington, Del.

A CHARMING SOUTHERNER —BUT ONE TOUGH COOKIE

His friends call him "Easy Ed." A small-town Southerner, Du Pont Co. CEO-designate Edgar S. Woolard Jr. is as comfortable making a pitch to a taciturn Dutch businessman as talking shop with a factory worker. But don't be misled. Underneath his personable shell, Woolard is one tough cookie. He proved himself a ferocious cost-cutter, and, on occasion, a staunch fighter of union organizers.

Woolard's friendliness has played well at consensus-oriented Du Pont. But as he takes over as chairman and CEO in April, some investors hope his tough side will dominate. At 55, Woolard is one of the youngest to get the top job at Du Pont. He is in a unique position to put the company on a more aggressive—and profitable—track.

Woolard comes from humble roots. He grew up in the sleepy town of Washington, N.C., where his father ran a combination luncheonette and pool hall. Voted "Most Likely to Succeed" in high school, he was the sort of boy who made it all look easy. Classmates say he was not particularly earnest in his studies, but he made top grades. He played intramural basketball and football at North Carolina State University and was known to pull plenty of fraternity pranks.

NOT BY THE BOOK. Almost on a whim, Woolard joined Du Pont in 1957 while on leave from the Army. As an industrial engineer, he was assigned to work as an efficiency expert. At first his only aim was to work near home. But his ambitions grew: He yearned to become plant manager some day. Wool-



THE FUTURE CHIEF (FAR LEFT)

ard accomplished that, and by 1978 he was tapped as head of the huge division making nylon, spandex, and other textile fibers. Just five years later he became a member of the company's powerful executive committee, and corporate president in 1987.

Woolard's rise to power has not been strictly by the book. Early in his career he raised eyebrows among top brass when a newspaper ran a photo of him in full Indian costume at a party. At a more recent masquerade party, he showed up as Boy George. Easy Ed's willingness to be unconventional may come in handy as he tries to put Du Pont on a more profitable course.

RON UNKEFER: SOMETIMES IT PAYS NOT TO HAGGLE



GOOD GUYS' UNKEFER: MAKING SWEET MUSIC WITH TOWER RECORDS

Less than three years ago it looked like bad times ahead for Good Guys Inc. Just as the tiny, Northern California consumer electronics chain opened five new stores, giant Circuit City Stores Inc. announced plans for nine outlets in the area. Good Guys' shares plunged from 18 to 2—about the price of a blank cassette.

Frightened, Good Guys founder and President Ronald A. Unkefer reexamined his business. One conclusion: California customers hated haggling over price, a common practice in the consumer electronics business. "The first television I ever sold, I gave the customer 10 bucks off," Unkefer wistfully recalls. Nonetheless, he junked the practice in favor of a more genteel approach—15% lower prices and a guarantee to match any competitor's price. He also improved staff training and stepped up advertising.

The tactics worked. Sales at stores open for one year rose 8% in 1988, four times the industry average. And for fiscal 1989, earnings are expected to jump 21%, to \$4 million, on sales of \$185 million. The company's stock has rebounded to about 9.

Unkefer hopes to keep the momentum by venturing outside Northern California with 10 new stores by the end of 1990—although he's keeping mum on the locations. Also ahead: electronics stores located adjacent to Tower Records shops, a national music chain. But expanding could stretch thin the Good Guys distribution system. And Circuit City, with sales of \$1.7 billion, could easily slash prices in Good Guys' markets. So far, however, the Good Guys are not finishing last.

By Robert D. Hof in San Francisco

COOK & PALMIOTTO HELP EXPORTERS GET A GOOD NIGHT'S SLEEP

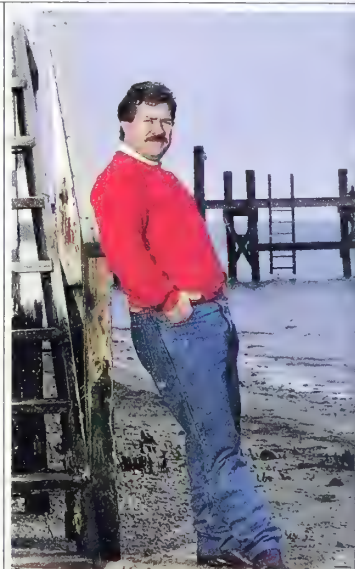
Thomas A. Cook and Antonio Palmiotto spotted a niche big insurance brokers had ignored. Five years ago the pair realized Americans were more interested than ever in doing business overseas. They figured small and midsize companies, new to the export game, would desperately need help arranging international risk management. They quit their jobs at the marine division of insurance broker Emmett & Chandler Co., borrowed \$500,000, and started their own firm, Cook & Palmiotto International Ltd.

Their timing couldn't have been better. Within six months

the Garden City (N.Y.) company was in the black on an operating basis. And when the dollar began its downward spiral in 1985 and U.S. exports boomed, Cook & Palmiotto was ready. It now helps its customers find the full array of insurance products necessary for doing business internationally—coverage for everything from shipping accidents to kidnappings. In addition to insurance, Cook & Palmiotto assists customers in lining up export credits or securing legal help. Today the burgeoning brokerage garners about \$55 million in annual premiums and employs 100 people in five offices around the country.

So far, Cook & Palmiotto remains tightly focused on pint-size customers. But it isn't thinking small. The typical company spends 1% to 3% of its foreign sales on this type of insurance, Cook says. With U.S. exports totaling \$320 billion last year, that adds up to annual premiums of \$3 billion to \$9 billion. Cook & Palmiotto is determined to grab a bigger piece of a very juicy pie.

By Robert Neff in New York



COOK INSURES INNOCENTS ABROAD

TRENDS

A SHRINKING LABOR POOL IS REALLY CRAMPING SMALL FRY

With the growth of the U.S. work force slowing, many businesses face labor shortages. But small businesses are feeling them first, says Jules H. Lichtenstein, head of the Small Business Administration's policy branch.

That's because small businesses employ two-thirds of all entry-level workers. And the number of Americans aged 16 to 24 is expected to shrink by more than 7%, to 31.5 million by the year 2000. And small employers tend to pay less, offer fewer benefits, and provide fewer chances for advancement than larger companies. Already, Northeast, Midwest, and West Coast companies can't fill some jobs.

The solutions? Long-term,

experts say better education and training will help by making each available worker more productive. For now, small employers will have to hike salaries and add such benefits as health and pension plans. Other remedies: luring new employees into the work force with flexible hours or customized compensation packages.

FEELING THE PINCH



DATA: NATIONAL FEDERATION OF INDEPENDENT BUSINESS



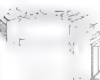
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PROFESSOR HARDBALL

BART GIAMATTI FACES A BIG-LEAGUE SQUEEZE PLAY
AS THE NEW COMMISSIONER OF BASEBALL



AND HERE'S
THE PITCH: A
BREWERS GAME



Bart Giamatti, a soft-spoken Italian Renaissance scholar, chuckles these days when he recalls how hard it was to explain to students the animosity between the medieval Guelphs and the Ghibellines, factions that battled for nearly two centuries over the supremacy of church or state.

The experience of getting to the nub of a dispute may soon prove invaluable. As he steps up from National League president to become the seventh commissioner of Major League Baseball on Apr. 1, Giamatti will have to do more than just analyze some long-simmering antagonisms among the sport's owners and players. He will have to cool them. Despite his academic demeanor, lifelong baseball fan Giamatti may well have to demonstrate anew the willingness he has shown in the past to play hardball when the times demand it.

Like many feuds, the situation that Giamatti faces is based on emotions as much as concrete issues. "The greatest problem in baseball today," he says, "can be expressed in one word: mistrust. Mistrust among owners, among players, mistrust of owners by players and owners by agents. It is corrosive." And these emotions are about to boil over because of the most common of catalysts: money.

BASEBRAWL? After enduring a spate of lean years in the early 1980s, baseball is rolling in money. Attendance is up, team paraphernalia are bringing in record revenues, and—most important—cable and network television are laying out vast sums to gain an advantage in the increasingly competitive world of broadcasting. Baseball has already enjoyed two consecutive years of operating profits amounting to \$100 million, in sharp contrast to the losses recorded as recently as 1985.

So why aren't the owners reveling in the unbridled optimism that goes with the opening of a new season? "It is too early to say that baseball is off and sailing into blue skies," says George Steinbrenner, principal owner of what may be the wealthiest team in baseball, the New York Yankees. "If you look deeper you are going to see some very dark, ominous clouds on the horizon." Indeed, baseball seems to be spoiling for a financial brawl: The players want a bigger share of the new riches. The less well-off teams fear coming up short in the bidding wars for top players. And several cities without major-league teams are hungry for a piece of the action.

These stresses could threaten baseball's long-cherished exemption from antitrust laws and set off a strike or lockout next season that would make the 51-day strike in the middle of the 1981 season seem like a seventh-inning stretch. There is telling evidence of how likely a strike is. Up to 25 of the star players who signed new contracts this season structured them to pay most of the money this season and in 1991. They will get smaller salaries in 1990 (chart, page 88). And the owners vow not to get caught flat-footed either. "I decided that the owners will not be vulnerable to going into a season threatened by a strike," says Barry Rona, the owners' chief labor negotiator. "So if negotiations fail by Feb. 15, we won't start spring training. That's what all this talk of a lockout is about."

AFTERNOON GAME. Into the middle of this maneuvering steps A. Bartlett Giamatti, 50, who loved the sport long before he was appointed to hold sway over it. His father, Valentine, was a literature professor at Mount Holyoke College, so Bart grew up in South Hadley, a western Massachusetts town so small that it didn't have a movie house. "About the only thing to do in summer was ride my bike and listen to Boston Red Sox games on the radio," he recalls. "I was probably 7 or 8 years old when my father and uncle took me to my first baseball game. I'd been listening on the radio often enough, but going to Fenway Park, I just was astonished at the whole thing."

Giamatti became a fan with a traditionalist's love of the game and its history. "I'm one of those people who thinks the best game is played in the afternoon on real grass in summer where every player is a generalist as well as a specialist," he

Cover Story

states. If it were up to him, there would be no designated hitters—typically aging players who take a turn at bat but not in the field.

Even after becoming a professor and then president of Yale University, Giamatti found time among his treatises on Dante and Spenser to publish broadsides on the integrity of the game. When the New York Mets traded one of their most popular players, pitcher Tom Seaver, to the Cincinnati Reds in 1977, Giamatti protested. The team's owners, he wrote in *Harper's* magazine, had lost "the ability to understand a simple crucial fact: that among all the men who play baseball there is, very occasionally, a man of such qualities of heart and mind and body that he transcends even the great and glorious game, and that such a man is to be cherished, not sold."

UMP BUMP. Giamatti resigned as president of Yale in 1986 with an eye toward returning to teaching. But then the National League owners offered him the presidency of the league—and a chance to put his sermons into action.

Last season, Giamatti slapped an unusually severe, month-long suspension on Reds manager Pete Rose, who had become a baseball immortal by breaking Ty Cobb's long-standing record for hits in a career. Rose's offense: bumping an umpire in a dispute over a call and touching off a near-

riot in the stands. The two things Giamatti hates most are disorderly crowds at baseball games along with gimmicky scoreboards that, instead of just giving information, incite disturbances.

Undoubtedly, Giamatti's first order of business as commissioner will be to hear recent allegations that Rose gambled in violation of league rules. He also may become involved in the case concerning Red Sox third baseman Wade Boggs, who is being sued by his former traveling companion, Margo Adams. This affair is certain to displease Giamatti, who wants baseball players to set a high moral tone. "Like it or not," he says, "players making large salaries have to accept being role models."

Rose's bumping penalty was not the first time Giamatti showed a willingness to take a tough stand. During a lengthy strike in 1984 and 1985 at Yale, he resolutely refused the workers' comparable worth demands, which meant raising the pay for female-dominated jobs. Despite protests by students and faculty, the Yale president insisted the strike was "a classic union struggle over wages."

The Yale episode is ominous. "Giamatti claimed he was pro-worker, but he didn't act that way," recalls Pat Carter, an organizer at Local 34 of the Hotel & Restaurant Employees union in New Haven. "The baseball players shouldn't expect any

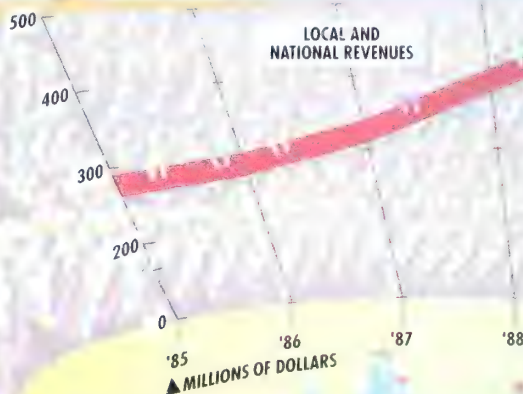
help from him. It would be a mistake they did." The strike eventually was settled when Yale agreed to establish the principle of comparable worth, although the university didn't give the union much more money.

When it comes to labor relations, the commissioner of baseball has less power than the president of Yale. The commissioner is supposed to be an impartial buffer between the owners and players, even though he is selected by the owners. For the record, Giamatti says: "I'm not going to do anything to stop a strike." But he soon adds in his typically understated whimsical manner: "If both sides want to come to me and say: 'Listen, we don't want a strike. We want to present the disagreement to you, and you in your wisdom adjudicate it,' wonderful. Then I perform and function brilliantly and superbly and everybody will be happy."

HIGHER STAKES. There is every indication that Giamatti's adjudicating skills will be called into play, because baseball's broad-based financial recovery has raised the stakes for both sides. Outgoing Commissioner Peter Ueberroth, who went to baseball fresh from his success running the 1984 Olympic Games in Los Angeles, has passed up no avenue for profits. He was surprised to find, for example, that Clette Co. paid virtually nothing for the rights to sponsor annual balloting for the

WHERE THE CASH FLOWS IN BASEBALL

BOUNTIFUL NEW BROADCASTING CONTRACTS..



Star Game, a privilege for which Gannett Co.'s *USA Today* now pays \$1 million a year. Expanding the licensing of apparel and other items pegged to baseball raised total sales to \$650 million last year from \$500 million in 1984. Baseball now clears \$1.1 billion from licensing fees.

The biggest benefits to baseball, however, have come from its traditional financial mainstay: broadcasting. Last December, the struggling CBS network, hungry for a huge audience that baseball play-offs and the World Series attract, raised the bid to \$1.1 billion over four years beginning in 1990. This bid—almost double the previous contracts with ABC and NBC—is for only 12 regular season games, the All-Star game, and the fall classics. In January, ESPN Inc. signed a four-year contract to broadcast 175 games each season, beginning in 1990. Total broadcast fees reaped by baseball for next year alone are estimated to amount to some \$650 million.

It's no wonder the value of a baseball franchise has soared. While the Reds sold for \$13 million earlier in the decade, and other teams had trouble even finding a buyer, "the value of baseball teams has improved across the board," says Mitchell S. Megna, vice-president at American Appraisal Associates Inc. and an expert on the value of sports teams. Today, Megna estimates, most small-market teams would bring \$60 million to \$80 million. "And you can't even put a value on

the big-market teams, like the Dodgers or the Yankees," he says. Anyone who wants to buy the Yanks, he volunteers, had better bring at least \$150 million to the table.

The overall broadcast fees mask some disparities within baseball, however. The Yankees, which play in the nation's biggest media market, earn some \$50 million a year from local broadcast rights. The Seattle Mariners earn \$3 million. And this is where things begin to get dicey. The Yankees and other big-market teams

Giamatti's first job: Looking into allegations that Pete Rose gambled in violation of league rules

can—and do—pay more to get top players, who draw the fans. So the less wealthy baseball teams are eager to curb the bidding for players. "If we don't do something to restrain the escalation in salaries, many teams will be in trouble in the not-too-distant future," says Carl Barger, president of the Pittsburgh Pirates.

It may come as no surprise that the players do not share Barger's sentiments. The teams had little trouble holding down salaries before 1976, because veteran players were not allowed to become free

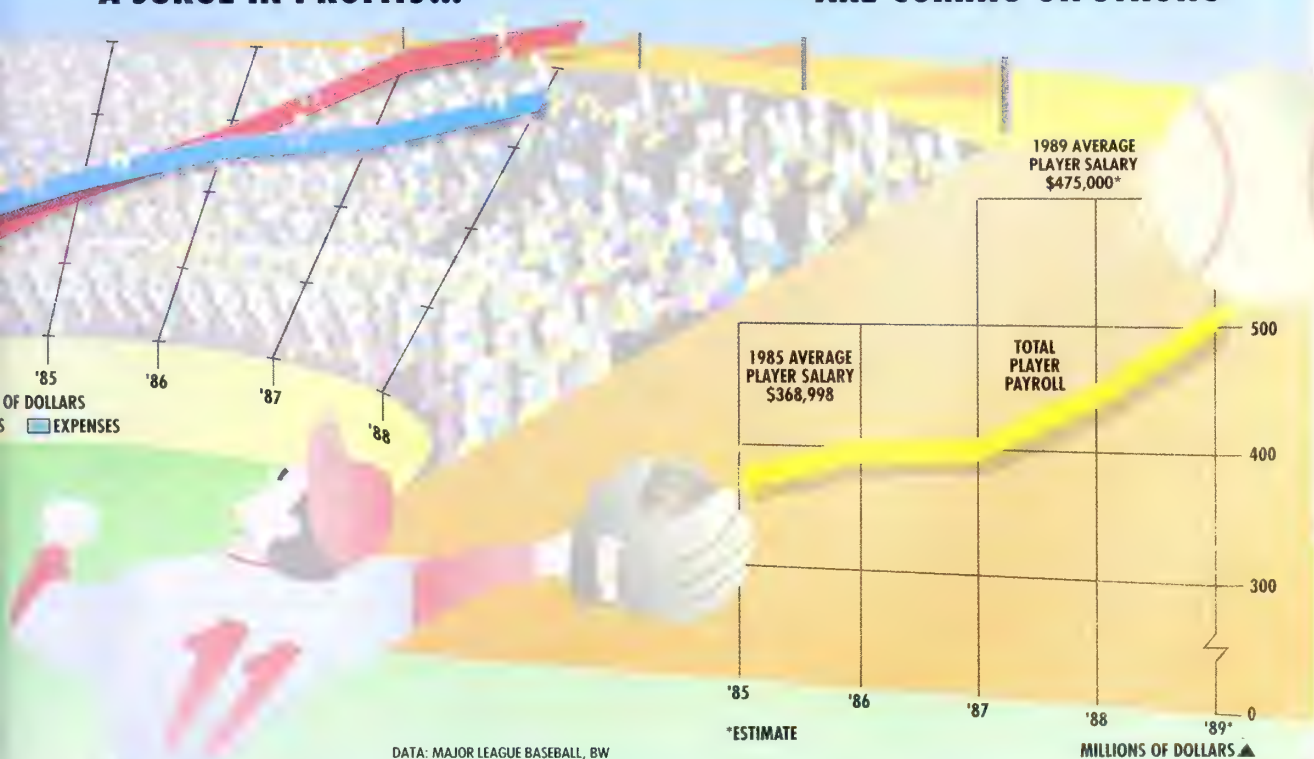
agents after their contracts expired. Free agency now permits a player to sell his services to the highest bidder. A player also is allowed, after three years in the big leagues, to demand a hearing before an arbitrator if he and his team disagree over his salary. The arbitrator considers what other players of similar skills earn and awards the player either his latest salary demand or the team's last offer—there is no middle ground. In gauging what other players earn, the arbitrator is supposed to look at players who have been in the majors for one year more than the player who lodges the protest. There is no appeal.

MILLIONAIRES' CLUB. Free agency and arbitration have created a more competitive market and produced those breathtaking salaries you read about. This year more than 100 players will earn at least \$1 million, and 20 players will top \$2 million. Baseball's highest-paid player, Los Angeles Dodgers pitcher Orel Hershiser, will earn \$2.8 million for his work this season—more than the entire payroll of the Mariners in the early '80s.

The owners tried to rein in salaries beginning in 1985, when they showed less willingness to bid for the top free agents. But since then an arbitrator has held that the owners unfairly colluded among themselves to hold salaries down. The owners face damages of up to \$120 million, even though they dispute the arbitrator's findings. Whatever the merits of the argument over collusion, the players' efforts to

...HAVE TOUCHED OFF A SURGE IN PROFITS...

...BUT PLAYER SALARIES ARE COMING ON STRONG



Cover Story

reopen the bidding process has paid off. The average major-league salary this year is expected to come in at around \$475,000, according to Rona, the owners' negotiator. That's up 11% from last year's levels—and four times the pace at which salaries increased from 1986 to 1988.

The current system of setting salaries has thus become the focus of talks under way to replace the existing contract, which expires on Dec. 31. "Without the current system of free agency and arbitration," says Joe Carter, the Cleveland Indians star center fielder who is playing a key role in the talks, "we'd go back to the days when only one or two players were making a million dollars or more." Referring

to the two-day strike in August, 1985, Paul Molitor, the Milwaukee Brewers third baseman who is also a central figure in the labor talks, declares: "In 1985 we were led to believe the game was about to go bankrupt. We were misinformed. This time we will fight to maintain what we have."

Donald M. Fehr, general counsel for the Major League Baseball Players Assn., thinks the owners may try to restrict or even eliminate free agency, something the players will not stand for. "If they've decided it's time to end free agency, come what may, they might consider a lockout despite the bad press it would give them," Fehr believes. "It doesn't make sense, because they have a lot of money. But I've

never found their negotiations to be founded on logic." Counters Rona: "If we are to meet our objective—which is to run baseball profitably—we will have to come up with a new means of setting salaries."

Although the players and the owners say they do not want a strike or a lockout in 1990, many privately fear that the season will never get started. "The talks have the potential to be very difficult, and I am concerned about next season," says Thomas S. Monaghan, president of the Detroit Tigers. He says he sees the possibility of strike or lockout next year. "But whatever happens," he adds, "I'm not giving in."

THE RUNAROUND. If he can avoid a strike or lockout, Giamatti faces yet another problem: expansion. Baseball has not added a franchise since 1977, and such cities as Washington, Denver, Phoenix, Miami, Tampa-St. Petersburg, and Buffalo are becoming impatient. So is Congress: The Senate has set up a Task Force on the Expansion of Major League Baseball, and many of the members are considering introducing legislation repealing the sport's unique antitrust exemption. The task force was created in November, 1987, as a result of the growing discontent on the Hill about baseball's failure to expand adequately.

Giamatti is "noodling" with hypothetical schedules that include two more teams in the National League, and he hopes to report back to Congress in July. He'll face many skeptics—among them Senator Dennis DeConcini (D-Ariz.), who is disgruntled with baseball's handling of the expansion issue.

Former Commissioner Ueberroth basically played a stalling game with the task force, he believes, adding: "Quite frankly, we've gotten the strong feeling that we're getting the runaround." DeConcini says that "if nothing comes of the July meeting, or it's a stall, I think the legislative options will be resurrected."

Giamatti remains patient: "If there's no expansion, there's got to be a labor agreement that prepares for it to be orderly and intelligent," he says. And there's plenty of time to get that agreement. "Each side has fundamental desires and needs they would view as imperative," says Giamatti. "My guess is if they could get past a certain amount of mistrust and divisiveness, they would have a much greater sense of overlap than it seems to me the public rhetoric has allowed us to see." If he can't dissolve that mistrust, Giamatti may go into the record books as the commissioner of baseball's most bitter season.

By Brenton Welling in New York and William C. Symonds at Spring Training in Arizona and Florida, with Aaron Bernstein in New York and Ron Stodghill in Washington

DO THE STARS FORETELL A STRIKE?

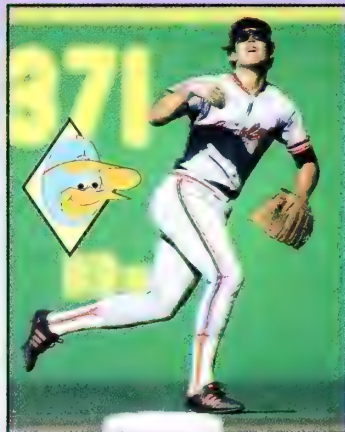
TO LIMIT THEIR LOSSES IN A STRIKE OR LOCKOUT, NEW CONTRACTS SIGNED BY STAR PLAYERS CONTAIN LESS MONEY FOR 1990. SOME EXAMPLES:

DWIGHT GOODEN P



SALARY '89 '90 '91
\$2,250,000 \$1,700,000 \$2,250,000

CAL RIPKEN JR. SS



SALARY '89 '90 '91
\$2,466,666 \$1,366,667 \$2,466,667

ANDY VAN SLYKE OF



SALARY '89 '90 '91
\$1,950,000 \$1,000,000 \$1,950,000

BRUCE HURST P



SALARY '89 '90 '91
\$1,733,333 \$1,633,333 \$1,883,334

TABLE 2. MINICOMPUTER RATINGS—RECAP BY VENDOR (Continued)

Manufacturers and Model	Total Minicomputers	Altos	AT&T Data Systems	Wang Laboratories	Digital Equipment Corp.	Hewlett-Packard	IBM	Siemens	Univac	Other
Survey Item										
Excellent (10) - Poor (1)										
Ease of Operation	8.4	7.4	7.3	8.0	8.0	8.1	8.7	8.4	8.2	8.4
Would Recommend System to Another User (%)										
Yes	91.0	72.7	92.3	97.7	91.4	93.1	96.3	76.2	82.1	86.8
No	2.7	4.5	3.0	1.7	3.9	3.9	2.8	14.3	2.6	2.6

IN THE FINAL ANALYSIS, NO OTHER MINICOMPUTER COMPANY COMES SO HIGHLY RECOMMENDED.

When over 97% of independently surveyed* Wang customers say they'd recommend Wang minicomputers to other users, that's a

CUSTOMER SATISFACTION

recommendation that's hard to beat.

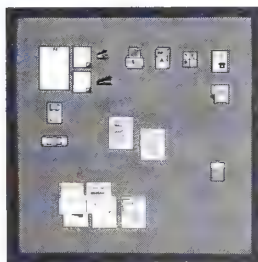
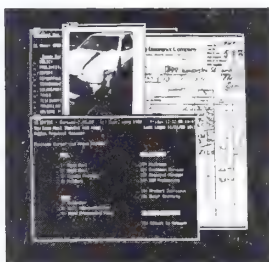
But maybe it's not all that surprising when you consider that Wang minicomputer systems also got top marks for ease of use, ease of conversion and for productivity aids that reduce programming costs.

It's nice to know that if you always put your customer first, the customer will often do the same for you.

WANG

MAKES IT WORK

Actual Wang computer screens shown here.



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FOR PETER COHEN, IT'S EVEN LONELIER AT THE TOP

A trio of high-level resignations leaves a big hole at Shearson

Peter J. Solomon was there at the beginning. A partner at the venerable Lehman Brothers Kuhn Loeb when Shearson acquired it in 1984, he bursts with pride when he talks about the firm's accomplishments since then. The Lehman connection made Shearson a takeover power on Wall Street. Mergers and acquisitions brought in a hefty \$300 million in fees last year. From 1984 to 1988, Solomon says the firm's M&A surge was "one of the most incredible success stories on Wall Street."

True. But Solomon, 50, won't be around to participate in the continuing saga of Shearson Lehman Hutton Inc. Neither will Daniel J. Good, 48, nor Francois de St. Phalle, 42. The trio had played a big role in Shearson's rise. But each resigned in March. Sources at Shearson say they all left primarily because of personality clashes with Chairman Peter A. Cohen or differences in business strategies.

SOLO ACT. An interview with Cohen for this story never materialized. A Shearson spokesman early in the week of Mar. 13 indicated that Cohen would be available for an interview. On Mar. 21, he said Cohen is on vacation with his family in Africa and unavailable for comment. The spokesman says: "The reasons for the resignations were mixed," and adds individuals had either "their own reasons" or left "as a result of mutual decisions."

Now the pressure is on Cohen, 42, to keep Shearson near the top of the megaprofit M&A business. And he must do so while adhering to the wishes of parent American Express Co., which wants Shearson to shy away from most hostile takeovers. This strategy could cause un-

rest among an ambitious staff that likes stalking such game. "The firm risks losing talent to smaller, seemingly more entrepreneurial competitors," notes Michael W. Blumstein, a First Boston Corp. analyst. And, with everyone's retail-sales business sagging, Shearson must rely even more on takeovers.

After arriving at Shearson in 1986,

charges in 1988. Shearson's \$146.5 million investment last year in MCorp., troubled Texas bank, could result in big loss.

Cohen had to fire James N. von Gmetten as president of Shearson's Boston Co. subsidiary after it overstated 1987 earnings by \$30 million. Most crushing, Cohen was blamed by the Street for

Shearson's failure to win control of RJR Nabisco Inc., missing out on \$200 million in fees. "RJR had to be a real disappointment to Cohen," says Samuel Hayes of the Harvard business school.

Cohen's decision to freeze out Solomon from the RJR negotiations embarrassed Solomon. "The facts are clear," Solomon says, "that for whatever reason, I had nothing to do with the RJR deal."

Cohen and Solomon had worked closely together. Cohen appointed him to run M&A in 1984 and co-manage investment banking a year later. Then in January, 1988, Cohen tapped Solomon to supervise a new merchant banking department. Solomon was also instrumental in helping



■ COHEN'S CHALLENGE: MAINTAINING M&A PROFITS IN SPITE OF AMEX' MISGIVINGS ON HOSTILE TAKEOVERS

Good ran its merchant banking operation. He has left to form a boutique called Good Capital Co. Solomon, a former co-head of investment banking, will do deals on his own for now. And de St. Phalle, who played a big role in Shearson's international capital markets effort, departed to run that business at Dillon, Read & Co.

The resignations come at a time when Cohen's once-stellar reputation seems to be dimming on the Street. Shearson's \$962 million takeover of E. F. Hutton & Co. in December, 1987, resulted in Shearson's \$165 million in nonrecurring

Shearson amass a \$1.35 billion fund to help finance leveraged buyouts. But there was a falling-out. Privately, Shearson officials say Solomon's breezy, ebullient personality clashed with Cohen's intense, aggressive style. A Shearson source adds that "Cohen needed Solomon's investment-banking expertise, but thought Solomon was given too much credit for Shearson's accomplishments." **'FED UP.'** The reason for de St. Phalle's resignation, say friends, was his dislike for Shearson's size. He preferred the quieter surroundings of Lehman Brothers, where he was a partner, and hated the

reocracy at Shearson. He was "fed" with the idea of asking a stream of lawyers for permission to do anything," says a source close to him.

In Good's case, Shearson initially slipped into his stable of raiders, which included Paul Bilzerian, Asher Edelman, and Edward De Bartolo. By advising Bilzerian on his 1988 hostile takeover of Renger Co., Shearson earned a fee of \$100 million, its biggest ever.

But Good was displeased when Cohen, lured by bad publicity in Beazer PLC's takeover of Pittsburgh-based Koppers, last year, suddenly shrank from doing unfriendly takeovers. "It was frustrating to Dan that we weren't interested in pursuing these kinds of clients," says a friend. As a result, Good was given less and less to do. Now Shearson will act "only on behalf of clients who are interested in owning the business," says James D. Robinson III, chairman of American Express. Robinson notes these clients are "few and far between."

HOLIDAY CHEER. Sources close to Shearson say Robinson and Cohen were at odds last year when Pennsylvanians, angry at Shearson-backed Beazer's takeover of Koppers, destroyed AmEx cards on television. Says Robinson: "Sure, it disturbed me." A former Shearson executive recalls sitting in Cohen's office when Robinson was talking on the phone about the Koppers takeover. At the point, he says, Cohen told Robinson: "You can't tell me how to run this firm. I'm running this firm." Robinson says, "Cohen never talked to me like that." Robinson calls Cohen the "best manager of anybody on Wall Street." And officials of the two companies, dismissing rumors that the two occasionally don't get along, note how Cohen and his family were the Robinsons' guests for the past Christmas holiday. "They're friends as well as business partners," says an AmEx official.

Yet when it was announced on March 3 that Louis V. Gerstner Jr. had suddenly resigned as president of American Express, Cohen was not chosen to succeed him. Instead, Robinson said he would take on the duties of the president. "A year ago, Peter would have been a prime candidate," says someone who knows both companies well.

Meanwhile, Shearson's M&A staff had a busy first quarter, without any business from the raiders. It is advising Time in its proposed \$9 billion merger with Warner Communications, Emhart in its \$2.8 billion acquisition by Black & Veatch, and the Prospect Group, which agreed to buy Illinois Central Transportation for \$440 million. With that streak, it may be wise to remember that Cohen has rebounded before. Few should be willing to bet against him now.

By Jon Friedman in New York

A PALL OVER THE FUTURES PITS? HELL, NO

Despite the sting, volume at Chicago's exchanges is soaring

You might think that the ongoing federal investigation of the trading practices in the Chicago futures pits would hang heavy over the exchanges, keeping customers on the sidelines and sending traders to unemployment lines. But you'd be wrong. Business at the Chicago Mercantile Exchange and the Chicago Board of Trade is booming.

Indeed, any doubts about a client getting a fair shake have been eclipsed by economic need. The recent credit tightening by the Federal Reserve Board and the runup in the government's inflation indexes are forcing companies to take cover and run to the futures markets.

tion was reported. It's even 6% higher than just prior to the news of the sting.

"Our seats are the most expensive in the futures industry," boasts William J. Brodsky, Merc president. He attributes part of the surge in seat prices to high hopes for the Merc's after-hours computerized trading system. Called Globex, it's scheduled to start trading late this year. The CBOT has developed a comparable system, called Aurora, which is not expected to be launched until 1990.

The biggest gains these days are in the Merc's Eurodollar pit, where average daily volume is running at 145,863 contracts, 90% over 1988 levels. Eurodollars are U.S. dollars on deposit at

A TRADING SURGE IN THE CHICAGO PITS

Increase in average daily volume*

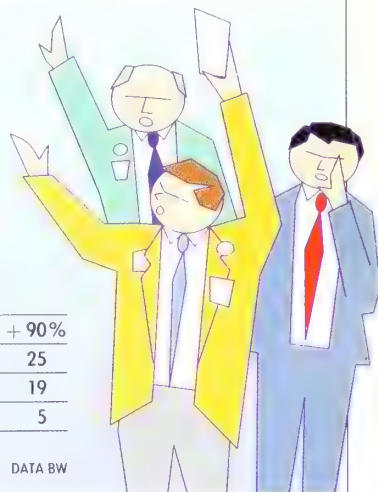
CHICAGO BOARD OF TRADE

U.S. TREASURY NOTES	+25%
CORN	14
U.S. TREASURY BONDS	9
SOYBEANS	9

CHICAGO MERCANTILE EXCHANGE

EURODOLLARS	+90%
JAPANESE YEN	25
SWISS FRANCS	19
LIVE CATTLE	5

*Futures contracts traded from January to mid-March, 1989, vs. the same period in 1988



DATA BW

"Businessmen are saying: 'I need to go and hedge myself. When this is all over, I'll sit down and talk about niceties,'" says S. Waite Rawls III, vice-chairman of Continental Bank Corp.

RECORD PRICE. Since mid-January—when news of the two-year Federal Bureau of Investigation sting operation was leaked—futures volume has soared. At the Merc, total trading volume from January through mid-March is up a huge 35% over the same period in 1988. At the CBOT, volume rose a strong 9% so far, and that's on top of a 12.5% gain in 1988, an all-time high.

Seat prices on the exchanges, perhaps the best barometer of the futures game, are climbing, too. A seat at the Merc recently sold for a record \$550,000, up 15% from a drop in the price after the Federal Bureau of Investigation opera-

banks outside the U.S., and each contract is the equivalent of a three-month, \$1 million time deposit. Banks and other lenders sell Eurodollar contracts to hedge their short-term borrowing costs. If short-term rates rise, a bank that "sold" time deposits in the Eurodollar futures market would see the value of its futures position rise and offset the higher cost of funds. Interest-rate woes have sparked increased trading at the CBOT's Treasury note and Treasury bond pits (table).

Trading is also picking up in the CBOT's soybean pit and the Merc's yen and Swiss franc pits, where the FBI probe was centered. Rawls sees the increased volume as confirmation that futures "is a pretty good game. At the minimum, it's the only game in town."

By Kathleen A. Behof in Chicago

BY GENE G. MARCIAL

IS AT&T LAYING THE CABLE FOR A HOOKUP WITH NCR?

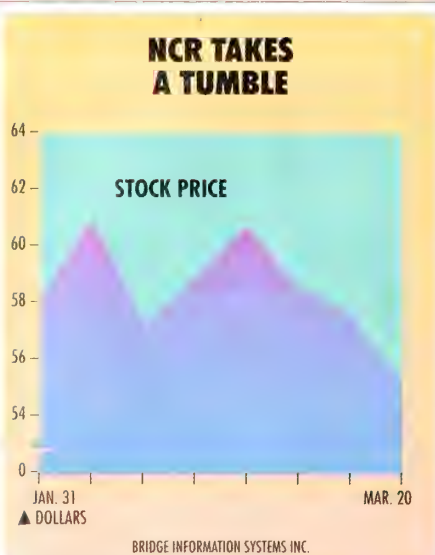
In recent weeks, NCR has been in a slump, falling to 54 after climbing as high as 61 in February. A quieting of takeover rumors drove the stock down, and IBM's disappointing earnings projections battered technology stocks.

But a number of big takeover players haven't given up on cash-laden NCR. They argue that the stock is way undervalued and is worth \$80 to \$120 a share. Plus, there are new whispers that NCR is a takeover target—of AT&T.

One money manager believes that NCR officers have had informal talks with bigwigs at the giant phone company. He speculates that the talks focused on a friendly AT&T acquisition of NCR, though other options were considered, too. One alternative would have AT&T buying a 20% stake and purchasing some NCR assets, possibly the manufacture of workstations designed for the retailing and financial industries, he says. These units, which contribute 20% of revenues, would dovetail nicely with AT&T's information processing operations. He adds that NCR's worldwide operations, roughly 55% of revenues, would be alluring because AT&T wants to expand its overseas business. Both companies declined comment.

NCR is currently trading at a low price-earnings multiple of around 9, well under that of IBM, Digital Equipment, and Hewlett-Packard. During the past three years it has traded at an average p-e of 13.5. NCR is expected to earn nearly \$6 a share this year, so a p-e of 13.5 would mean a price of \$81. **DONE DEALS.** NCR is even more undervalued when compared with the buyout prices of other computer companies. A number of deals in the industry have been based on a price of 8 to 10 times operating cash flow. At 8 to 10 times NCR's estimated 1989 operating cash flow of \$12.08 a share, NCR's stock would have a value of \$97 to \$121.

Don Smalter, a senior analyst at I3D Research, figures NCR should generate close to \$2 billion, or \$25 a share, in free cash flow over the next three years. That would be enough to repurchase up to 33 million shares, or 40% of the outstanding stock at current prices. NCR has been an active buyer of its own shares. This year it plans to repurchase up to 10 million shares.



Smalter says one unrecognized NCR asset is its 70% stake in its Japanese subsidiary, NCR Japan. The holding is carried on NCR's books at \$600 million. Based on its current price on the Tokyo Stock Exchange, Smalter figures that NCR's stake in NCR Japan is worth about \$2 billion, or \$20 a share. With or without a takeover, NCR could spin off its Japanese stake and use the cash to buy back more shares.

Smalter believes that NCR's highly regarded management, led by Chairman and CEO Charles Exley Jr., wouldn't be averse to a good offer. Exley subscribes to a strategy of maximizing shareholder value, he says, "as opposed to empire building."

HUFFY'S SUITORS ARE PEDALING FAST

Gerry Angulo, managing director at First Capital Partners, teaches a course on takeovers at Columbia University. He usually discusses only done deals in the classroom, leaving aside the live, undervalued catches for his own business pursuits. One company that he thinks will provide fodder for future classes—and whose shares he has started to buy in real life—is Huff, the nation's largest bicycle maker, with about 25% of the market.

Big players have been converging on Huff. The New York investor group Odyssey Partners has accumulated a 4.4% stake, and Invesco Capital Management owns 8.1%. More recently some arbitrageurs have started buying the stock, which is trading at 15%. In January, when Angulo first noticed

Huff, the stock was selling at 18. "The company is cheap based on its strong cash flow, well-known brand and leadership in the sports-equipment market," says Angulo. About 10% of Huff's production goes to K mart. Although the bike market was soft last year, sales have started to pick up, and earnings are expected to jump to about \$1.35 a share—the highest in almost 10 years—vs. 1988's \$1.07.

Based on estimated 1989 free cash flow of \$30 million, or \$3.75 a share, Angulo figures the stock is worth nearly \$30 a share. With little debt, the company is an ideal candidate for a leveraged buyout, he says. Management, led by Chairman and CEO Harry Shaw III, holds a 6% stake. Huff has been repurchasing shares and plans to buy back up to nearly 5%. Angulo says that if a raider comes in, management may be forced into an early LBO.

THIS SKYLINE IS DRAWING CROWDS

Most housing and building stocks have been in the dumps, depressed mainly by rising interest and mortgage rates. But Skyline is going in the opposite direction. A leading maker of manufactured, or mobile, homes and recreational vehicles (RVs), Skyline's sales are expected to climb to about \$365 million from last year's \$322.9 million. And for the first half of fiscal 1989, which ended on May 31, sales of manufactured homes alone are expected to jump about 20%. Sales of RVs, which have been depressed for years, are also on the comeback trail, notes one analyst.

With the stock selling at 18, the company's market capitalization is only \$198 million. That's cheap, says one New York investment manager who has been buying shares, considering that the company has free cash flow of about \$105 million, or \$10 a share. With working capital of \$120 million and practically no debt, "there's a good chance that the company will get raised," says the money manager, who puts Skyline's breakup value at about \$30 a share. He believes a real estate group is accumulating shares.

Another big investor expects management to come under pressure to use its free cash to repurchase shares. "Another alternative, of course, is for management to undertake a leveraged buyout," he says. Insiders own 17% of the stock, some 13% of which is held by Chairman and CEO Arthur Decio.

BATTERIES NOT INCLUDED.



You can spend \$500,000 on an elaborate fire protection system. But if you neglect to replace a \$50 battery somewhere in that system, you may not be fully protected.

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THE GIANTS RETRENCH

LOWERING THEIR SIGHTS HAS MONEY CENTER BANKS ON THE MEND

To be known as "a money center bank" was, for many years, the financial equivalent of a nation being known as a superpower. The money centers conducted themselves accordingly, proudly marching out of their U.S. strongholds to conquer country after country. Closer to home, they boldly planned for the day when new laws would let them vanquish regional banks and securities firms across the U.S.

Now that they have led U.S. banking into a humbling series of world-class lending disasters, from Third World regimes to Texas oil rigs, the money center banks are competing with each other to abandon the role. Some want to be seen as superregionals, like, say, Charlotte's NCB Corp. or Pittsburgh's PNC Financial. Others, frustrated with the shrinking returns in just-plain banking, want to be investment banks.

It's not hard to see why. Few regionals were badly burned in Third World adventures, and they've prospered from the mundane, such as car loans and mortgages. And the dream of big returns in securities is still compelling despite the tepid market. As they changed their stripes, many money centers saw a spectacular earnings rebound in 1988 (page 96). It's far from clear, though, that they can sustain their profits from U.S. consumers—or defend their global base against further inroads by Japanese and European banks.

The money centers still play their customary role of gathering funds from smaller banks across the U.S. and then lending them to big borrowers. But even the most successful corporate bankers, such as J.P. Morgan & Co. and Bankers Trust New York Corp., are narrowing their focus to niches of corporate finance, such as takeover lending and hedging strategies. Says Howard Schneider, president of BT Securities Corp.: "Coke is probably the only company that can be all things to all people."

ESCAPE FROM NEW YORK. Others are making far more wrenching adjustments. Jettisoning its global ambitions, Bank of America—once the nation's largest—has shrunk back to being a California retail bank. Manufacturers Hanover Corp. describes itself as a regional with a global wholesale business. Chemical Banking Corp. is a super-regional, with bases in Texas and the New York City area.

Profit-hungry New York bankers are even leaving their Manhattan palaces for humbler digs. Chase Manhattan Corp. is moving its back-office staff to Brooklyn, and Chemical may move from Park Avenue to a proposed development in Times Square. Citicorp has sold most of its trademark midtown tower—while retaining the right to picture it in ads—to a Japanese insurer. This year it will move its retail business across the East River to—gulp—Queens. It's a one-stop subway ride, but to Richard S. Brad-dock, the chief of Citi's Individual Bank, it means crossing "the widest river in the world."

Clearly, Wall Street doesn't mind: Large banks were among last year's best-performing stock groups. And in mid-March with Treasury Secretary Nicholas F. Brady's plan to backstop more of their Third World lending, share prices of money centers set or at least neared postcrash highs.

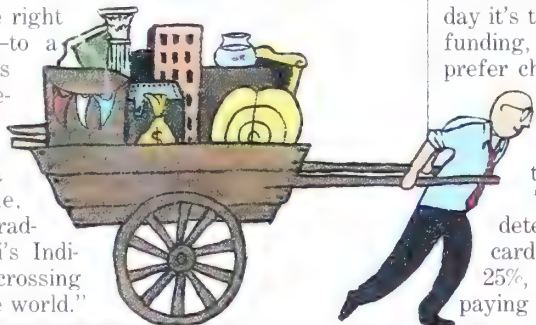
The role model for the two biggest U.S. banks, Citi and Chase, is now American Express Co., for its skillful wooing of the upscale consumer. "You could switch whole layers of management between us and AmEx today, and nothing would change," says one senior Citi officer. Between AmEx and Chase, asserts Chase President Thomas G. Labrecque, "there's no difference in structure."

► **CITICORP** has sold most of its trademark building in Manhattan to a Japanese insurer and will halve its rent bill by relocating its retail headquarters to a new tower in Queens

The resurgence of retail is apparent in the balance sheets. Four years ago, Citi carried \$3 in commercial loans for every \$2 in consumer debt on its books. Today it's the reverse. For funding, big banks now prefer cheap, stable de-

posits over borrowing from money markets. And since regulators view home mortgages as safer than corporate loans, banks need only half as much capital to back home mortgages.

The allure of retail is powerful. Despite the risks of deteriorating credit, Citi is still pushing hard in credit cards. Last year its U.S. card base reached 23 million, up 25%, and charges hit \$23 billion, up 30%. Manny Hanny is paying \$65 million to buy 11 branches in New York City.



and \$1.2 billion in deposits—from a troubled thrift. Chemical's costly purchases of Texas Commerce Bancshares Inc. and New Jersey's Horizon Bancorp. gave it \$3.7 billion in deposits in Texas and many tail and small-business customers in New Jersey.

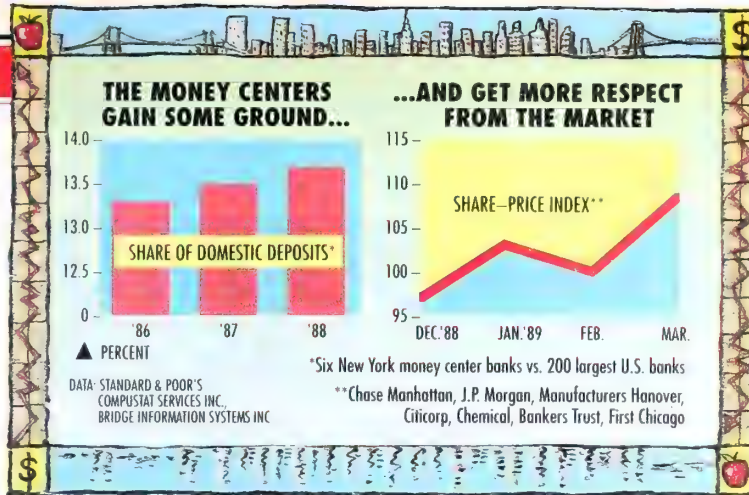
MARGIN SQUEEZE. Nonetheless, the money centers have far to go in building global consumer bases. Although credit cards are still highly profitable, bankers face a margin squeeze as their lending costs rise. Citi's enormous mortgage business, based in St. Louis, felt the same pain as other mortgage bankers last year. And so far neither Citi nor Chase has profited from any of the regional banks and ailing thrifts each has bought in Florida, California, and other states.

Citi's aggressive push in European consumer banking faces stiff resistance from such giants as Deutsche Bank, which is now adding insurance to its vast arsenal of products. In Japan, Citi has only seven of the 100 branches it wants, and is adding just

IN MANHATTAN

ing most of its
office operations
Wall Street to
development site
town Brooklyn.
iti, it's hustling
pscale customers

e per year. Citi says it's willing to buy or join with a Japanese bank, but the price is high. With the Japanese moving to Europe and Europeans to the Far East," says Citi's Braddock, "retail banking is looking more and more attractive to everyone." The U.S. money centers aren't giving up on corporate loans. Banks are still writing more corporate loans—but instead of keeping them, they sell them off. Bankers Trust has written more than \$60 billion in leveraged buyout loans since 1985 but is kept only \$4 billion. Says Morgan President Dennis Weatherstone: "You can use your capital more effectively by increasing the turnover of assets than just getting bigger." Although that brings juicy fee income, margins on loans themselves are minute. Citi offered to finance Eastman Kodak's purchase of Sterling Drug Inc. at just 0.13 percentage

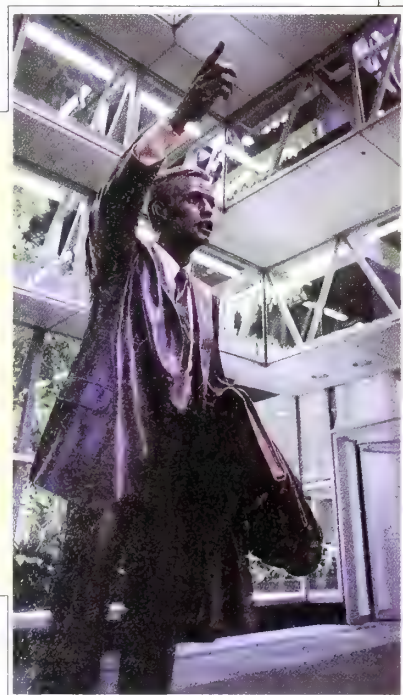


point over the cost of funds to banks. Even so, it lost, because Bankers Trust would take only 0.10 point. Banks command bigger spreads on loans to LBOs, but these entail greater credit risk and increase the volatility of earnings. If it made no new LBO loans, Bankers Trust estimates that its net could fall by as much as 20%. Meanwhile, large U.S. companies are turning

more to foreign banks for their loans, according to consultants Greenwich Associates. Although Japanese firms have so far stayed with conventional, low-margin loans, their huge edge in assets and capital could help them "do in financial services what they did in autos," says George J. Vojta, executive vice-president at Bankers Trust. They may attack U.S. retail banking, too. From a sizable base in California, such Japanese banks as Sanwa Bank California are already issuing JCB credit cards to some of their U.S. customers.

To beat back foreign rivals, banks want new securities powers. But even as they get them, banks may not find them profitable. Citi lost \$164 million in London equities last year and expects to lose \$50 million more in

► **CHEMICAL**, which is
thinking of leaving its
Park Avenue digs,
now sees itself as a
superregional, with
strongholds in Texas and
the New York-New Jersey
metropolitan area



1989. "We made some dumb mistakes," says Citi's investment banking chief, Michael A. Callen. "But we think we're ahead of the field in fixing them." Perhaps. But if banks rush into new markets in the U.S. as they did in London, profits in U.S. investment banking may plunge. Asks Citi's London capital markets chief, Brian P. Woolley: "Will the U.S. market go the way of Europe? I think it will."

In investment banking, most U.S. banks have already lowered their sights. "We can't go after the blue-chip customers of Salomon or Nikko; we'd get our clocks cleaned," says Douglas E. Ebert, executive vice-president of investment banking at Manny Hanny. He and other bankers think they can do well by serving medium-size and smaller companies. But that means poaching on the turf of strong regional banks, who want new powers, too. Although the money centers are riding higher right now, their period of adjustment is far from over.

By Frederic A. Miller in New York, with bureau reports

THE BANKS REFILLED THEIR MONEYBAGS IN 1988

THEY BOOSTED EARNINGS HANDSOMELY—AND THE PARTY ISN'T OVER

If 1987 was a year that bankers would rather forget, 1988 was one they might be very happy seeing all over again. Last year was far more successful than even the most optimistic bankers had dreamed.

A look at BUSINESS WEEK's annual Bank Scoreboard, which begins on page 98, shows the scale of the improvement. While assets rose a scant 1.7% at the nation's 200 largest banks, the industry earned a total of \$18.9 billion last year after taxes. That's a dramatic change from the \$2.1 billion loss they posted in 1987, and 47% above their 1986 net. Fundamental measures of bank performance also rebounded: Return on assets rose to 0.83%, compared with a loss of 0.13% in 1987 and a 0.6% ROA in 1986. And the average return on equity for the top 200 reached a respectable 15.7% last year, a far cry from 1987's -2.5% and also above the 11.4% in 1986.

EGGED ON. Reported earnings were boosted by special factors. Large banks had fallen into the red in 1987 after adding \$32.9 billion to reserves against possible losses on Third World debt. That drastic move, led by Citicorp, created the opportunity for some huge rebounds by generating tax-loss carryforwards that directly benefited 1988's earnings. Furthermore, Brazil decided to end its debt-service moratorium last year, paying overdue interest for 1987 and much of 1988 in the fourth quarter. Many banks took that payment directly into earn-

ings. And some of the biggest banks realized onetime gains selling off buildings and businesses.

Banks were under great pressure to generate earnings any way they could get them—and retain a sizable chunk on their own books. Egged on by federal regulators to improve their balance sheets, the top 200 banks boosted their capital by nearly one-quarter of a percentage point, 5.26% of assets. Even some banks hardest hit by the 1987 losses say they will easily meet the regulators' 1989 capital targets.

Investors liked the rebound. The combined market value of the top 200 banks has risen 14% from the depressed levels of March, 1988. Just as the 25 largest banks fared farther than most stock groups in 1987's October crash, they recovered more vigorously, too, zooming 34% in the past 12 months. And although bank share prices generally gave up some ground in the fourth quarter, the big banks still wound up beating the overall stock market last year.

HAPPY GIANT. Will the improvement last? With special factors less likely to raise reported earnings this year, some large banks may show a slight decline in profits. But analysts at Keefe, Bruyette & Woods Inc. expect income per share for the 163 banks it follows to rise by 12.5% in 1989. The reason: Banks are continuing the same cost-cutting disciplines that were forced on them after 1987.

Take BankAmerica Corp. Even after adjust-

THESE BANKS SCORED 1988'S BIGGEST GAINS...

	Adjusted earnings per share*	
	1987	1988
COLORADO NAT'L BANKSHARES	\$0.05	\$0.98
VALLEY NATIONAL	0.33	3.41
AMOSKEAG BANK SHARES	0.17	1.45
BANKAMERICA	0.51	3.64
COLONIAL BANCORP	0.25	1.22
EQUIMARK	0.64	2.21
AMERITRUST	0.89	2.62
CONTINENTAL BANK	1.04	2.87
FIRST PENNSYLVANIA	0.51	1.36
UNION PLANTERS	0.73	1.71

...AND THESE SUFFERED THE SHARPEST SETBACKS

	Adjusted earnings per share*	
	1987	1988
MCORP	\$-6.47	\$-19.40
FIRST BANK SYSTEM	3.45	-5.10
AFFILIATED BANKSHARES	0.75	-0.41
INDEPENDENCE BANCORP	2.63	-1.04
SUNWEST FINANCIAL SERVICES	3.30	0.25
BALTIMORE BANCORP	1.67	0.15
FIRST FIDELITY BANCORP	2.95	0.29
NATIONAL BANCORP OF ALASKA	2.74	1.04
FIRST AMERICAN	2.42	1.32
SOUTHEAST BANKING	3.29	2.26

*Aside from Third World loan-loss provisions, the resulting tax benefits, and large asset sales. Sample includes top 163 banks.

DATA: KEEFE, BRUYETTE & WOODS INC.

for special factors in 1988 and 1987, BofA's earnings rose more than 600% (ble). The bank's debt was upgraded by Moody's Investors Service Inc. on Mar. 20, and its stock price has tripled since its low in January, 1988. BofA managed to restore earnings by pruning up its huge California branch system, pruning its loan portfolio, and slashing overhead. Although the company is still laboring under a \$9 billion load of loans to developing countries, Wall Street is betting that BofA should still show 10% or better growth in earnings per share this year. At the other extreme, Valley National Bancorp, a Clifton (N.J.) bank, posted a hefty 2.04% return on its \$1.7 billion in assets, the highest ROA in the BUSINESS WEEK Bank Scorecard for the second year in a row. After 61 consecutive years of earnings increases, Valley expects profits to rise 10% once more in 1989. The bank avoids speculative office-building loans in the overbuilt New Jersey market, says President Peter Guthway, and carries mostly adjustable-rate mortgages in its residential portfolio. But if rates keep rising, some of its mortgage payments will reach their lifetime caps,

One problem: If rates keep rising, 'the delinquency problem in ARMs is really going to hurt'

squeezing Valley's handsome 5% net interest margin.

Over time, rising rates may mean more credit problems at the 9 million households with ARMs. Fleet/Norstar Financial Group Inc. in Providence, R. I., says that delinquency rates on the \$750 million in ARMs it services for other banks have risen from 3% to 4.5%. "The delinquency problem in ARMs is really going to hurt in 1989 and 1990," predicts H. Jay Sarles, executive vice-president. Other Northeast banks, such as First Fidelity Bancorp in Newark, N. J., have reported real estate problems that worry investors.

So far, however, there are few signs that a real estate disaster such as the one that devastated many Sunbelt banks and S&Ls will swamp the country. Some banks even see opportunity there: At yearend, Miami-based Southeast Banking Corp. bought a troubled thrift in Jacksonville, despite the resulting hit to earnings. If the banking industry can get through both the thrifts and the Third World without much more carnage, there could be many more good years ahead.

By Frederic A. Miller in New York

WHAT THE COLUMN HEADINGS MEAN

Market value

Closing share price of a bank's common stock on Mar. 10, 1989, multiplied by the corporation's latest available number of common shares outstanding

Assets

Total assets as of Dec. 31, 1988

Deposits

Total deposits as of Dec. 31, 1988. Interest-bearing deposits and noninterest-bearing deposits together will total 100%. Foreign deposits subtracted from 100% will equal total domestic deposits

Loans

Aggregate face value of all outstanding loans and leases as of Dec. 31, 1988, net of unearned income and before deduction of valuation allowance and loan loss reserves

Provision for loan loss

Charge for anticipated loan losses, which appears on the income statement as an operating expense

Net charge-offs as percent of loans

Net charge-offs less recoveries as percent of net average loans outstanding. A minus sign indicates that recoveries exceed charge-offs

Operating income

Operating income after minority interests and taxes but before preferred dividends, and gains and losses from the sale of securities

Net income

Net income after minority interests and taxes

Return on assets

Net income available for common shareholders (net income minus preferred dividends) divided by average assets

Leverage

Average assets divided by average common equity computed on a daily average basis for the year ended Dec. 31, 1988

Return on equity

Net income available for common shareholders divided by average common equity for the year ended Dec. 31, 1988. Return on average assets multiplied by leverage equals return on average common equity

Net interest income

Total interest income adjusted for tax equivalents minus total interest expense before provision for loan losses

Growth in earnings per share

Annual trend in the growth rate of primary earnings per share for the restated five-year period ended Dec. 31, 1988

ALPHABETICAL LIST OF BANKS

Number following each bank's name is its asset ranking in the tables beginning on the next page

ankings 139 anc 199 rust 49 eag Bank 154 th Bancorp. 61 Banc-Corp 175 ne 24 Popular 82 klahoma 157 p of Hawaii 71 p of Miss. 194 sumi le Israel 123 f Boston 14 f New England 15 f New York 10 f Tokyo Trust 67 hires 167 outh 94 merica 3 s Trust New York 9 f Iowa 143 ide-America 155 nce 132 Banks 23 iks 57 inancial 99	Boatmen's Bancshares 39 Boulevard Bancorp 188 CDE CB&T Bancshares 164 Central Bancshares 104 Central Fidelity Banks 97 Central Jersey Banc. 189 Chase Manhattan 2 Chemical Banking 6 Chemical Financial 200 Citicorp 1 Citizens & Southern 32 Citizens Bancorp 172 Citizens Banking 150 Citizens First 138 City National 101 Citytrust Bancorp 141 CNB Bancshares 195 Colorado National 134 Comerica 46 Commerce Bancshares 85 Commonwealth Bk. 193 Constellation Banc. 160 Continental Bank 17 CoreStates Financial 36 Crestar Financial 51 Cullen/Frost Bankers 117 Dauphin Deposit 119 Deposit Guaranty 112	Dominion Bancshares 59 EquiMark 118 Equitable Bancorp. 89 European American 86 Exchange Bancorp. 136 FG Fifth Third Bancorp 88 First Alabama Banc. 90 First American (Tenn.) 65 First American (D. C.) 50 First Bancorp. Ohio 125 First Bank System 26 First Capital 131 First Chicago 12 First Citizens 115 First City Texas 42 First Commerce 103 First Commercial 185 First Eastern 147 First Empire State 79 First Florida Banks 92 First Hawaiian 102 First Illinois 177 First Interstate (Calif.) 8 First Interstate (Wis.) 183 First Maryland Bancorp 75 First Midwest Banc. 166 First National (Ga.) 198 First Natl. Cincinnati 83 First of America Bank 54	First Pennsylvania 74 First Security 91 First Tennessee Natl. 76 First Union 21 First Virginia Banks 95 First Wachovia 29 Firststar 63 FirstTier 153 Fleet/Norstar 20 Florida National 64 Fort Wayne National 187 Fourth Financial 13 Fuji Bank & Trust 93 Fulton Financial 191 Grenada Sunburst 178 HII Harris Bankcorp 45 Hawkeye Bancorp. 197 Hibernia 80 Huntington Bancshares 56 IBJ Schroder Bank 114 Imperial Bancorp 146 Independence Banc. 133 Indiana National 78 Industrial Bank Japan 96	Integra Financial 68 Israel Discount Bank 100 Jefferson Bankshares 190 KLM Key Centurian Banc. 162 KeyCorp 40 Keystone Financial 144 Landmark Banc. 168 LaSalle National 121 Liberty National 122 Lincoln Financial 156 Magna Group 161 Manufacturers Hanover 7 Manufacturers Natl. 58 Mark Twain Banc. 170 Marshall & Ilsley 69 Mellon Bank 16 Mercantile Banc. (Mo.) 72 Mercantile Bk. (Md.) 110 Merchants National 87 Meridian Bancorp 55 Michigan National 44 Midlantic 33 Midwest Financial 152 Mitsui Mfg. 179 MNC Financial 35	Moore Financial 107 Morgan (J. P.) 4 Multibank Financial 130 N National Texas 145 National City 31 National Commerce 181 National Community 111 National Westminster 34 NBD Bancorp 27 NCNB 18 NESB 184 New Hamp. Savings 182 North Fork Bancorp 180 Northeast Bancorp 116 Northern Trust 53 Norwest 30 OP Ohio Bancorp 186 Old Kent Financial 62 Old National Bank 169 One Valley W. Va. 173 PNC Financial 13 Premier Bancorp 105	Provident Bancorp 165 Puget Sound Banc. 106 QRS Republic New York 25 Riggs National 66 Sanwa Bank 73 Security Bancorp 142 Security Pacific 5 Shawmut National 22 Signet Banking 47 Society 52 South Carolina Natl. 84 Southeast Banking 37 Southern National 140 SouthTrust 70 Sovran Financial 28 State Street Boston 60 Statewide Bancorp 163 Sumitomo Bank 108 Sumcorp 149 Summit Bancorp. 113 SunTrust Banks 19 SunWest Financial 127 T Texas American Banc. 98	Trustcompany Banc. 176 Trustcorp 77 UV U. S. Bancorp 41 U. S. Trust 124 Union Bank 38 Union Planters 120 United Banks Colo. 81 United Carolina 158 United Jersey Banks 48 United Missouri 109 UST 151 Valley Banc. (Wis.) 128 Valley Capital (Nev.) 148 Valley National (Ariz.) 43 Valley Natl. (N. J.) 174 Victoria Bankshares 192 WXYZ Washington Banc 159 Wells Fargo 11 WestAmerica Banc 196 Whitney Holding 135 Wilmington Trust 126 Worthern Banking 171 Zions Bancorp. 129
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BANKS

ASSETS

DEPOSITS

LOANS

		12/31/88 \$ MIL.	12/31/88 \$ MIL.	CHANGE FROM 1987	INTEREST/ NONINT.	FOR- EIGN	12/31/88 \$ MIL.	CHANGE FROM 1987	
1	CITICORP	New York	207666	124072	4	86/14	49	149197	8
2	CHASE MANHATTAN	New York	97455	64057	-7	75/25	45	69602	2
3	BANKAMERICA	San Francisco	94647	77150	1	77/23	23	69022	7
4	MORGAN (J. P.)	New York	83923	42469	-3	86/14	70	28324	-8
5	SECURITY PACIFIC	Los Angeles	77870	47653	5	75/25	13	55465	7
6	CHEMICAL BANKING	New York	67349	47966	-14	72/28	14	41590	-16
7	MANUFACTURERS HANOVER	New York	66710	41714	-8	81/19	44	49024	-12
8	FIRST INTERSTATE BANCORP	Los Angeles	58194	44149	18	71/29	2	37799	16
9	BANKERS TRUST NEW YORK	New York	57942	32491	8	76/24	59	24115	-8
10	BANK OF NEW YORK	New York	47388	32706	91	75/25	35	33061	103
11	WELLS FARGO	San Francisco	46616	35069	9	80/20	4	37670	2
12	FIRST CHICAGO	Chicago	44432	32018	2	80/20	41	27874	-1
13	PNC FINANCIAL	Pittsburgh	40811	27453	14	83/17	5	24028	17
14	BANK OF BOSTON	Boston	36061	23591	5	81/19	24	26457	8
15	BANK OF NEW ENGLAND	Boston	32200	24623	6	82/18	13	24939	13
16	MELLON BANK	Pittsburgh	31153	21325	-1	80/20	15	18984	-6
17	CONTINENTAL BANK	Chicago	30578	16967	-14	83/17	38	16577	-18
18	NCNB	Charlotte, N. C.	29848	20670	6	81/19	4	18908	11
19	SUNTRUST BANKS	Atlanta	29177	23944	6	77/23	NA	20101	9
20	FLEET NORSTAR FINANCIAL GROUP	Providence	29052	20701	9	79/21	6	19748	12
21	FIRST UNION	Charlotte, N. C.	28978	20033	15	79/21	3	18924	23
22	SHAWMUT NATIONAL	Hartford	28414	18988	-1	74/26	4	18971	8
23	BARNETT BANKS	Jacksonville, Fla.	25748	22482	11	86/14	0	19369	14
24	BANC ONE	Columbus, Ohio	25274	19502	7	83/17	0	17325	11
25	REPUBLIC NEW YORK	New York	24519	16346	10	95/5	48	5724	3
26	FIRST BANK SYSTEM	Minneapolis	24248	17204	9	80/20	8	16131	21
27	NBD BANCORP	Detroit	24176	19495	7	79/21	8	14683	11
28	SOVRAN FINANCIAL	Norfolk, Va.	22484	17493	5	80/20	2	15308	11
29	FIRST WACHOVIA	Winston-Salem	21815	16492	15	74/26	4	13719	11
30	NORWEST	Minneapolis	21750	13902	2	77/23	1	14348	11
31	NATIONAL CITY	Cleveland	21623	16906	11	79/21	4	14314	9
32	CITIZENS & SOUTHERN	Atlanta	21098	16082	7	74/26	0	14099	9
33	MIDLANTIC	Edison, N. J.	19697	15793	16	79/21	1	15513	19
34	NATIONAL WESTMINSTER BANCORP	New York	19013	15663	64	79/21	12	13390	63
35	MNC FINANCIAL	Baltimore	18015	12309	10	82/18	6	12901	13
36	CORESTATES FINANCIAL	Philadelphia	16431	11115	8	69/31	13	10965	8
37	SOUTHEAST BANKING	Miami	15823	11505	9	81/19	4	9971	11
38	UNION BANK	Los Angeles	15010	11911	143	61/39	4	11029	160
39	BOATMEN'S BANCSHARES	St. Louis	14676	11224	-2	75/25	0	8918	7
40	KEYCORP	Albany, N. Y.	14646	11581	14	78/22	0	9324	18
41	U. S. BANCORP	Portland, Ore.	14383	10168	7	77/23	0	9676	12
42	FIRST CITY BANCORP. OF TEXAS	Houston	12195	9843	NA	80/20	4	7176	NA
43	VALLEY NATIONAL	Phoenix	11766	9512	-2	80/20	0	7803	-2
44	MICHIGAN NATIONAL	Farmington Hills	11306	9214	34	84/16	4	7437	24
45	HARRIS BANCORP	Chicago	11276	8849	8	68/32	22	6545	9
46	COMERICA	Detroit	11145	9250	10	82/18	1	6916	16
47	SIGNET BANKING	Richmond, Va.	11002	7546	-1	82/18	1	6907	2
48	UNITED JERSEY BANKS	Princeton, N. J.	10886	8894	13	76/24	0	7317	11
49	AMERITRUST	Cleveland	10738	8359	8	82/18	3	7427	4
50	FIRST AMERICAN BANCSHARES	Washington, D. C.	10640	8380	9	76/24	2	6551	12

a. Includes and excludes: a. Data are for bank's operations only. b. Loans are net of unearned income only. c. Total interest income net of adjustments for tax equivalent. d. Includes preferred stock. e. Banking operations are fully adjusted. f. Income net of adjustments for securities gains or losses. g. Since April 1988. Deposit and loan data for prior year are not restated for 1988. h. NA = Not Available.

E B O A R D

PERFORMANCE

MARKET VALUE

NET CHARGE- OFFS AS % OF LOANS	OPER. INCOME 1988 \$ MIL.	NET INCOME 1988 \$ MIL.	RETURN ON ASSETS 1988 %	LEVER- AGE 1988	RETURN ON EQUITY 1988 %	NET INTEREST INCOME 1988 \$ MIL.	CHANGE FROM 1987 %	NET INCOME AS % OF NET INT. INCOME	5-YEAR AVER. GROWTH EPS %	3/11/89 \$ MIL.	CHANGE FROM 1988 %	RANK
1.2	1698.0g	1698.0	0.77	27.8	21.4	7697	19	22.1	10.3	8217	32	1
1.1	1039.9	1058.9	1.52	18.3	27.8	3413	7	31.0	17.9	2898	35	10
0.3	547.0g	547.0	0.51	33.1	16.8	3703	22	14.8	NM	3896	151	4
0.0	1001.8g	1001.8	1.20	16.0	19.1	2042	9	49.1	-6.6	6391	4	2
1.8	644.3	638.9	0.82	23.1	18.9	2714	12	23.5	-33.9	4355	32	3
0.7	735.4	753.6	0.91	30.6	27.7	2500	13	30.1	13.6	1962	46	21
1.6	940.4	751.6	0.96	30.5	29.4	2048	2	36.7	17.8	1681	27	25
2.3	130.8	102.4	0.16	28.6	4.7	2476	11	4.1	-17.5	2097	3	17
0.1c	647.7g	647.7	1.12	18.0	20.3	1021	14	63.5	NM	3112	19	8
1.0	191.9	213.0	0.78	20.0	15.6	806	15	26.4	2.9	2730	186	12
0.8	515.0	512.5	1.09	22.1	24.0	1997	8	25.7	0.4	3429	24	6
1.9	513.1g	513.1	1.05	28.0	29.3	1217	-1	42.2	27.7	2251	72	16
0.7	425.5	442.7	1.18	16.4	19.3	1261	14	35.1	12.9	3612	5	5
0.8	314.6	322.3	0.91	20.1	18.3	1172	-2	27.5	-17.0	1719	13	24
1.2	269.2	281.7	0.93	20.0	18.6	1150	9	24.5	11.1	1618	-19	28
3.0	-69.0	-65.0	-0.34	33.9	-11.7	889	-4	-7.3	NM	794	6	43
0.8	316.3	315.8	0.91	28.9	26.4	656	6	48.1	NM	1021	23	37
0.8	242.5g	252.5	0.86	18.1	15.5	979	7	25.8	7.9	2936	74	9
0.9	309.1	308.7	1.13	15.4	17.4	1243	5	24.8	12.5	2727	-4	13
0.5	327.9	335.8	1.21	15.0	18.1	1234	10	27.2	10.3	2766	13	11
0.6	319.2	296.9	1.06	15.2	16.2	1173	1	25.3	14.3	2273	-1	15
0.6	242.5g	242.5	0.91	16.9	15.3	1030	3	23.5	8.8	1830	7	23
0.5	226.4	226.4	0.94	17.5	16.4	1048	7	21.6	16.5	2070	4	18
1.0	332.9	340.2	1.44	12.3	17.7	1142	5	29.8	12.9	3231	21	7
0.2	136.8	169.7	0.59	24.1	14.3	458	9	37.0	-9.4	1337	2	32
0.7	-310.0	-310.0	-1.22	20.3	-24.9	625	-16	-49.6	NM	1254	-6	33
0.4	226.6	227.2	0.97	16.5	16.1	833	6	27.3	17.5	1854	17	22
0.5	236.3	243.1	1.14	15.7	17.9	856	3	28.4	13.5	2004	3	19
0.8	241.4	244.3	1.22	14.1	17.2	811	4	30.1	8.7	2329	13	14
2.0	221.1	211.2	0.98	19.7	19.3	904	11	23.4	15.1	1599	29	29
1.2	226.6	233.2	1.18	15.6	18.4	861	7	27.1	11.6	1966	63	20
0.5	203.0	206.3	0.96	18.1	17.4	832	6	24.8	12.7	1653	30	26
0.5	222.4	222.9	1.20	14.9	17.9	828	10	26.9	12.3	1516	0	30
0.6	131.3	97.9	0.56	13.2	7.4	677	56	14.5	NA	NM*	NM	NM
0.8	183.1	170.2	0.99	16.8	16.6	676	10	25.2	21.1	1351	16	31
0.7	166.8	179.5	1.14	14.7	16.7	719	6	25.0	13.1	1628	9	27
0.7	75.3	75.3	0.49	21.6	10.6	533	3	14.1	-6.6	771	7	45
0.9	96.5	60.2	0.77	17.9	13.7	374	32	16.1	17.1	769	NM	46
0.8	68.4	69.8	0.47	14.2	6.7	507	1	13.8	-0.5	1101	44	34
0.6	114.3	119.9	0.86	16.7	14.4	603	12	19.9	8.1	920	23	40
0.6	122.2	123.9	0.92	15.0	13.8	557	14	22.2	13.5	1079	3	36
2.1	66.1g	66.1	0.42	31.6	13.2	312	NA	21.2	NA	397	NM	90
1.4	66.8	62.3	0.61	18.5	11.3	466	2	13.4	3.5	548	-4	69
0.8	91.5	93.2	1.04	16.5	17.3	408	8	22.8	35.4	673	-6	56
0.5	88.5	90.1	0.79	16.0	12.6	395	13	22.8	17.1	NM*	NM	NM
0.5	113.4	112.0	1.04	18.3	19.0	423	5	26.5	15.6	738	9	47
1.4	143.6	152.5	1.35	18.6	25.1	440	6	34.7	6.3	813	6	42
0.4	114.5	116.1	1.08	14.6	15.7	463	7	25.1	12.4	956	3	39
0.9	105.9	103.5	1.02	13.4	13.7	391	29	26.5	12.2	844	20	41
0.4	77.9	74.8	0.74	14.7	10.9	365	18	20.5	NA	NM*	NM	NM

**With adjustments, total deposits grew 2.4% and loans, 3%.

NA=not available. NM=not meaningful. NR=not reported. * Due to ownership structure

DATA: STANDARD & POOR'S COMPUSTAT SERVICES INC.

BANKS C

ASSETS

DEPOSITS

LOANS

		12/31/88 \$ MIL.	12/31/88 \$ MIL.	CHANGE FROM 1987 %	INTEREST/ NONINT. %	FOR- EIGN %	12/31/88 \$ MIL.	CHANGE FROM 1987 %	
51	CRESTAR FINANCIAL	Richmond, Va.	10408	7982	9	79/21	0	7451	3
52	SOCIETY	Cleveland	10010	7676	5	80/20	3	6254	9
53	NORTHERN TRUST	Chicago	9904	6753	-1	71/29	14	4666	18
54	FIRST OF AMERICA BANK	Kalamazoo, Mich.	9769	8675	15	83/17	0	6244	15
55	MERIDIAN BANCORP	Reading, Pa.	9523	7125	8	82/18	0	6152	12
56	HUNTINGTON BANCSHARES	Columbus, Ohio	9506	7107	8	81/19	1	5882	11
57	BAYBANKS	Boston	9496	7900	10	78/22	1	7569	19
58	MANUFACTURERS NATIONAL	Detroit	9311	7868	9	79/21	9	6150	9
59	DOMINION BANCSHARES	Roanoke, Va.	9204	7082	12	84/16	1	6262	13
60	STATE STREET BOSTON	Boston	8372	5388	19	48/52	21	2179	2
61	AMSOUTH BANCORP.	Birmingham, Ala.	8313	6511	11	82/18	0	5364	7
62	OLD KENT FINANCIAL	Grand Rapids	7854	6505	11	84/16	2	4685	13
63	FIRSTAR	Milwaukee	7842	6293	4	75/25	1	4988	5
64	FLORIDA NATIONAL BANKS OF FLORIDA	Jacksonville	7828	6090	2	81/19	0	4600	2
65	FIRST AMERICAN	Nashville	7204	5818	6	82/18	2	4501	10
66	RIGGS NATIONAL	Washington, D. C.	7015	5554	6	84/16	35	3563	7
67	BANK OF TOKYO TRUST	New York	6946	5498	3	86/14	55	3685	4
68	INTEGRA FINANCIAL	Titusville, Pa.	6927	5777	2	85/15	0	4059	5
69	MARSHALL & ISLEY	Milwaukee	6775	5211	2	75/25	0	4075	13
70	SOUTHRUST	Birmingham, Ala.	6645	5119	6	83/17	1	4077	13
71	BANCORP HAWAII	Honolulu	6635	5662	15	82/18	12	4088	21
72	MERCANTILE BANCORP.	St. Louis	6459	5309	-2	79/21	1	4644	-1
73	SANWA BANK	San Francisco	6430	5139	22	80/20	15	4443	18
74	FIRST PENNSYLVANIA	Philadelphia	6407	4757	15	72/28	10	4296	14
75	FIRST MARYLAND BANCORP	Baltimore	6274	4352	6	73/27	4	4427	15
76	FIRST TENNESSEE NATIONAL	Memphis	5972	4657	3	75/25	0	3579	-1
77	TRUSTCORP	Toledo	5947	4472	2	86/14	0	4027	11
78	INDIANA NATIONAL	Indianapolis	5927	4303	9	77/23	2	3841	13
79	FIRST EMPIRE STATE	Buffalo	5908	5057	16	90/10	7	3967	14
80	HIBERNIA	New Orleans	5834	4729	15	83/17	8	4238	29
81	UNITED BANKS OF COLORADO	Denver	5812	4624	6	75/25	3	3110	0
82	BANCO POPULAR DE PUERTO RICO	San Juan	5661	4716	5	78/22	0	3057	12
83	FIRST NATIONAL CINCINNATI	Cincinnati	5657	4723	13	83/17	0	3886	15
84	SOUTH CAROLINA NATIONAL	Columbia	5655	4028	17	79/21	0	3810	11
85	COMMERCE BANCSHARES	Kansas City, Mo.	5444	4683	5	76/24	0	3003	12
86	EUROPEAN AMERICAN BANCORP	New York	5335	4385	-3	71/29	3	3351	-16
87	MERCHANTS NATIONAL	Indianapolis	5256	3757	18	77/23	1	2999	25
88	FIFTH THIRD BANCORP	Cincinnati	5246	4094	18	81/19	0	3754	27
89	EQUITABLE BANCORP.	Baltimore	5245	3517	6	79/21	5	2975	21
90	FIRST ALABAMA BANCSHARES	Montgomery	5174	4332	16	81/19	0	3170	17
91	FIRST SECURITY	Salt Lake City	5159	3903	1	82/18	1	3680	8
92	FIRST FLORIDA BANKS	Tampa	5132	4328	6	78/22	0	3558	13
93	FUJI BANK & TRUST	New York	4910	3232	2	97/3	91	1861	8
94	BANK SOUTH	Atlanta	4881	3552	14	77/23	0	3260	8
95	FIRST VIRGINIA BANKS	Falls Church	4796	4223	8	81/19	0	3191	13
96	INDUSTRIAL BANK OF JAPAN TRUST	New York	4748	3090	-4	98/2	82	2097	32
97	CENTRAL FIDELITY BANKS	Richmond, Va.	4731	3744	11	84/16	0	3212	9
98	TEXAS AMERICAN BANCSHARES	Fort Worth	4383	4227	-6	81/19	0	3280	-18
99	BB&T FINANCIAL	Wilson, N. C.	4377	3552	13	84/16	1	3030	14
100	ISRAEL DISCOUNT BANK (b)	New York	4311	3966	10	97/3	37	1126	8

Footnotes on page 98

E B O A R D

PERFORMANCE										MARKET VALUE		
NET CHARGE-OFFS AS % OF LOANS	OPER. INCOME 1988 \$ MIL.	NET INCOME 1988 \$ MIL.	RETURN ON ASSETS 1988 %	LEVERAGE 1988	RETURN ON EQUITY 1988 %	NET INTEREST INCOME 1988 \$ MIL.	CHANGE FROM 1987 %	NET INCOME AS % OF NET INT. INCOME	5-YEAR AVER. GROWTH EPS %	3/11/89 \$ MIL.	CHANGE FROM 1988 %	RANK
1.0	87.9	86.7	0.83	17.5	14.5	379	0	22.8	3.6	724	2	49
0.4	98.5	100.1	1.05	14.9	15.6	379	7	26.4	12.7	771	7	44
2.5	109.3	109.3	1.12	25.8	28.9	256	13	42.7	42.4	717	14	50
0.4	89.0g	88.8	0.78	19.5	15.1	393	12	22.6	11.1	484	-5	77
0.3	172.0	86.1	0.94	13.5	12.7	366	5	23.5	11.9	733	6	48
0.9	87.9	87.6	1.01	16.1	16.2	349	4	25.1	14.8	697	-1	53
0.2	88.4	88.5	1.02	16.2	16.6	378	11	23.4	16.4	674	4	55
0.4	96.1	96.3	1.06	17.1	18.0	333	6	28.9	-5.6	678	7	54
0.7	84.2	83.0	0.96	16.0	15.4	362	7	22.9	14.0	710	12	51
0.5	91.7	92.3	1.27	14.7	18.7	216	-3	42.8	16.8	981	5	38
0.3	78.1	79.8	1.00	15.7	15.7	275	6	29.0	9.8	597	-4	63
0.2	77.2	77.1	0.98	15.6	15.4	283	13	27.3	12.9	570	11	67
2.7	133.4	132.3	1.76	16.7	29.4	317	14	41.8	27.4	615	23	60
1.0	35.5	34.9	0.46	16.2e	7.5e	301	0	11.6	-6.9	638	69	57
1.4	30.4	30.4	0.43	15.1	6.5	273	5	11.1	-2.5	495	-4	74
0.6	37.0	37.0	0.59	18.9	11.1	174	14	21.3	-22.8	351	9	96
0.5	36.9	37.2	0.52	21.3	11.0	127	16	29.4	NA	NM*	NM	NM
0.5	61.4	66.4	1.00	13.0	13.0	277	5	24.0	13.0	608	98	62
0.1	75.7	76.2	1.20	13.5	16.2	248	-1	30.8	11.2	632	23	58
0.3	67.0	67.6	1.08	14.9	16.1	243	9	27.8	13.2	556	7	68
0.3	74.8	74.9	1.25	15.9	19.9	249	18	30.0	15.7	609	27	61
3.4	27.0	28.7	0.44	15.1	6.7	236	-8	12.1	-8.6	446	27	81
0.5	31.5	31.8	0.55	16.0	8.8	210	23	15.1	NA	NM*	NM	NM
0.6	55.3	58.2	0.89	25.9	23.2	236	15	24.7	47.1	485	28	76
0.7	52.7	52.4	0.89	15.2	13.5	269	4	19.4	15.2	702	73	52
1.2	52.1	52.3	0.90	16.5	14.8	234	5	22.3	6.4	407	5	87
1.4	6.9	1.3	-0.03	15.4	-0.5	224	9	0.6	NM	342	-2	98
1.6	55.7	55.8	1.06	14.1	15.0	205	9	27.2	2.7	518	7	72
0.2	46.0	44.5	0.83	14.3	11.8	195	2	22.8	37.9	386	11	91
0.8	53.0g	53.0	1.00	17.2	17.1	210	7	25.2	15.3	492	13	75
1.7	9.0	9.0	0.12	14.6	1.8	220	-8	4.1	-31.2	211	-5	130
1.1	47.0	47.1	0.85	17.4	14.9	264	14	17.9	8.5	385	33	92
0.5	55.3	55.4	1.06	12.6	13.3	216	10	25.7	8.1	571	-4	66
0.4	54.1	54.5	1.05	14.1	14.8	239	1	22.9	11.3	459	4	79
0.0c	47.5	49.0	0.97	13.7	13.2	188	2	26.1	8.6	417	27	83
-0.5	97.6	64.9	1.20	17.1	20.4	238	5	27.3	NA	NM*	NM	NM
0.9	44.3	44.1	0.97	14.2	13.7	172	10	25.6	7.7	404	14	88
0.5	84.3	84.2	1.80	10.0	18.0	204	14	41.3	16.7	1091	45	35
0.6	54.6	48.2	0.78	24.3	18.9	198	3	24.3	26.1	316	-5	105
0.4	58.2	58.2	1.24	10.7	13.3	202	5	28.9	6.5	541	6	70
0.9	33.1	33.0	0.66	13.3	8.7	210	9	15.7	3.7	313	3	106
0.3	49.3	48.9	0.99	13.5	13.3	206	-1	23.7	7.2	452	2	80
0.0	12.2	11.6	0.26	19.9	5.1	34	4	34.2	NA	NM*	NM	NM
0.4	43.2	43.4	0.96	16.5	15.8	193	8	22.5	9.0	362	7	94
0.2	60.9	60.9	1.32	11.8	15.6	219	1	27.8	9.1	573	9	64
0.2	16.4	15.4	0.39	17.2	6.6	63d	45	24.5	-22.7	NM*	NM	NM
0.5	48.4	49.5	1.15	13.1	15.0	189	-1	26.2	10.3	428	-2	82
4.3	-510.2	-510.3	-10.35	276.2	NM	93	-44	NM	NM	6	-85	180
0.3	38.8g	38.7	0.95	15.5	14.7	165	-1	23.4	9.6	323	17	101
0.4	17.2	17.3	0.42	18.8	7.9	77	19	22.5	NA	NM*	NM	NM

BANKS

ASSETS

DEPOSITS

LOANS

		12/31/88 \$ MIL.	12/31/88 \$ MIL.	CHANGE FROM 1987 %	INTEREST/ NONINT. %	FOR- EIGN %	12/31/88 \$ MIL.	CHANGE FROM 1987 %	
101	CITY NATIONAL	Beverly Hills, Calif.	4296	3465	24	68/32	0	2438	23
102	FIRST HAWAIIAN	Honolulu	4239	3774	11	83/17	5	2384	24
103	FIRST COMMERCE	New Orleans	4166	3383	17	76/24	0	2076	12
104	CENTRAL BANCSHARES OF THE SOUTH	Birmingham, Ala.	4109	2810	15	81/19	0	2585	14
105	PREMIER BANCORP	Baton Rouge, La.	4078	3529	-4	80/20	0	2327	-2
106	PUGET SOUND BANCORP	Tacoma, Wash.	3947	2751	9	83/17	0	3029	13
107	MOORE FINANCIAL GROUP	Boise, Idaho	3906	3035	14	81/19	0	2196	14
108	SUMITOMO BANK OF CALIFORNIA	San Francisco	3719	3319	0	87/13	21	2767	15
109	UNITED MISSOURI BANCSHARES	Kansas City	3714	3110	0	66/34	0	1382	8
110	MERCANTILE BANKSHARES	Baltimore	3642	3011	11	76/24	0	2623	12
111	NATIONAL COMMUNITY BANK	Rutherford, N. J.	3614	3079	14	70/30	0	2757	19
112	DEPOSIT GUARANTY	Jackson, Miss.	3571	2840	5	80/20	0	2159	7
113	SUMMIT BANCORP.	Summit, N. J.	3526	2964	14	81/19	0	2506	11
114	IBJ SCHRODER BANK & TRUST	New York	3422	1584	11	87/13	38	1401	14
115	FIRST CITIZENS BANCSHARES	Raleigh, N. C.	3410	2990	11	79/21	0	1860	14
116	NORTHEAST BANCORP	Stamford, Conn.	3394	2684	5	76/24	0	2372	8
117	CULLEN/FROST BANKERS	San Antonio	3386	2851	8	81/19	0	1565	-4
118	EQUIMARK	Pittsburgh	3353	2837	10	88/12	0	2443	4
119	DAUPHIN DEPOSIT	Harrisburg, Pa.	3336	2546	4	86/14	0	1592	3
120	UNION PLANTERS	Memphis	3269	2419	18	82/18	0	1863	11
121	LASALLE NATIONAL (i)	Chicago	3182	2681	115	80/20	1	1977	83
122	LIBERTY NATIONAL BANCORP	Louisville	3163	2575	22	81/19	1	2124	25
123	BANK LEUMI LE ISRAEL	New York	3140	2826	8	84/16	19	1999	13
124	U. S. TRUST	New York	3061	2526	24	62/38	4	939	-3
125	FIRST BANCORP. OF OHIO	Akron	3049	2648	17	82/18	0	1732	25
126	WILMINGTON TRUST	Wilmington, Del.	2982	2291	-4	82/18	0	2045	15
127	SUNWEST FINANCIAL SERVICES	Albuquerque	2964	2551	14	85/15	0	1591	15
128	VALLEY BANCORP.	Appleton, Wis.	2958	2576	5	84/16	0	1863	12
129	ZIONS BANCORP.	Salt Lake City	2931	2280	-2	79/21	3	1645	-6
130	MULTIBANK FINANCIAL	Quincy, Mass.	2901	2370	9	81/19	0	2175	15
131	FIRST CAPITAL	Jackson, Miss.	2895	2422	4	79/21	0	1780	11
132	BANPONCE	San Juan	2842	2519	4	85/15	0	1721	5
133	INDEPENDENCE BANCORP	Perkasie, Pa.	2826	2332	11	86/14	0	1689	24
134	COLORADO NATIONAL BANKSHARES	Denver	2811	2278	8	74/26	0	1719	4
135	WHITNEY HOLDING	New Orleans	2747	2267	-1	68/32	0	1551	8
136	EXCHANGE BANCORP (i)	Chicago	2738	2154	34	77/23	4	1580	25
137	FOURTH FINANCIAL	Wichita	2693	2217	4	77/23	0	1458	16
138	CITIZENS FIRST BANCORP	Glen Rock, N. J.	2678	2390	17	84/16	0	1941	20
139	AFFILIATED BANKSHARES COLORADO	Denver	2617	2236	3	79/21	0	1494	1
140	SOUTHERN NATIONAL	Lumberton, N. C.	2601	2212	12	83/17	0	1729	9
141	CITYTRUST BANCORP	Bridgeport, Conn.	2600	2214	6	85/15	0	2113	0
142	SECURITY BANCORP	Southgate, Mich.	2575	2329	5	87/13	0	1483	6
143	BANKS OF IOWA	Des Moines	2494	2038	8	79/21	0	1409	19
144	KEYSTONE FINANCIAL	Harrisburg, Pa.	2456	2143	6	88/12	0	1591	9
145	NATIONAL BANCSHARES TEXAS	San Antonio	2449	2393	-7	79/21	0	1571	-13
146	IMPERIAL BANCORP (i)	Los Angeles	2428	2054	40	46/54	0	1240	33
147	FIRST EASTERN	Wilkes-Barre, Pa.	2400	2078	17	86/14	0	1669	20
148	VALLEY CAPITAL	Las Vegas, Nev.	2386	1977	10	67/33	0	1488	18
149	SUMMCORP	Fort Wayne, Ind.	2368	2023	15	85/15	0	1640	23
150	CITIZENS BANKING	Flint, Mich.	2354	1935	2	83/17	0	1438	11

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E B O A R D

PERFORMANCE										MARKET VALUE		
NET CHARGE-OFFS AS % OF LOANS	OPER. INCOME 1988 \$ MIL.	NET INCOME 1988 \$ MIL.	RETURN ON ASSETS 1988 %	LEVER-AGE 1988	RETURN ON EQUITY 1988 %	NET INTEREST INCOME 1988 \$ MIL.	CHANGE FROM 1987 %	NET INCOME AS % OF NET INT. INCOME	5-YEAR AVER. GROWTH EPS %	3/11/89 \$ MIL.	CHANGE FROM 1988 %	RANK
0.2	49.3	49.3	1.41	16.2	22.8	163	19	30.3	24.0	626	23	59
0.1	43.1	43.3	1.08	18.0	19.4	163	16	26.6	14.8	461	45	78
1.1	24.1	23.5	0.55	19.8	10.9	150	7	15.7	-12.5	204	6	132
0.4	39.7	41.0	1.05	14.4	15.1	148	2	27.7	9.4	311	6	107
3.1	-48.6	-49.7	-1.20	15.3	-18.4	147	-17	-33.8	NM	120	-2	164
0.2	40.3	40.4	1.08	14.4	15.6	140	10	28.8	3.8	346	14	97
0.6	25.6	25.5	0.72	15.5	11.2	127	12	20.0	-3.4	250	24	116
0.3	25.5	24.5	0.73	19.1	13.9	137	11	17.9	13.6	144	-11	149
0.4	30.8	34.5	1.00	11.7	11.6	127	8	27.2	5.3	340	-1	99
0.1c	53.3	53.4	1.59	10.0	15.8	163	11	32.8	11.5	517	14	73
0.1	59.6	42.0	1.25	18.9	23.6	161	19	26.2	25.2	364	-6	93
0.9	31.9	31.5	0.92	14.9	13.7	138	-8	22.9	8.8	257	-6	115
0.1	36.8	38.7	1.14	14.4	16.4	148	7	26.1	13.5	411	13	86
0.5	8.6	8.8	0.22	12.0	2.7	51	19	17.3	NA	NM*	NM	NM
0.3	21.2	21.2	0.66	15.3	10.1	127	-1	16.7	0.7	278	-8	112
0.4	33.9	34.6	1.09	12.9	14.0	132	6	26.2	11.0f	527	67	71
1.5	1.7	2.4	0.07	18.9	1.4	102	5	2.4	-43.8	125	64	161
1.4	25.0	25.3	0.69	24.0	16.5	142	26	17.8	39.7	130	-3	156
0.4	39.3	40.7	1.31	12.2	16.0	113	2	35.9	12.7	402	17	89
0.7	24.9	25.6	0.83	13.9	11.6	108	9	23.8	5.0	219	26	126
0.1a	28.4	28.4	0.83a	18.2a	15.2a	95	76	29.8	70.4	NM*	NM	NM
0.3	28.8	28.9	1.00	14.4	14.3	112	13	25.8	12.9	281	8	111
0.4	12.0	12.0	0.42	19.7	8.2	104	8	11.5	3.8	NM*	NM	NM
1.2	29.9	30.6	1.22	13.5	16.4	94	-13	32.5	NA	411	-8	85
0.3	35.2	35.2	1.31	10.8	14.2	118	-1	29.7	9.0	302	-3	108
0.3	50.0	51.8	1.87	13.5	25.2	115	8	45.0	24.5	572	13	65
1.1	23.3	23.3	0.81	14.5	11.8	118	2	19.7	6.6	282	3	110
0.3	26.7	26.5	0.96	13.5	12.9	114	2	23.2	6.5	295	24	109
2.3	-13.6	-17.9	-0.64	16.1	-10.2	114	2	-15.6	NM	138	-6	152
0.2	26.1	26.9	1.01	15.0	15.2	116	11	23.1	6.7	221	7	125
0.5	26.2	27.5	0.98	13.8	13.5	113	1	24.3	14.3	226	-8	123
1.1	19.6	21.8	0.70	18.8	13.2	104	7	20.9	4.6	143	12	150
0.2	11.1	-10.4	-0.36	15.7	-5.7	94	-11	-11.1	NM	230	-6	122
1.0	10.6	10.6	0.40	14.4	5.7	116	3	9.1	-37.2	166	26	146
1.0	25.8	25.8	0.96	9.9	9.5	113	-2	22.9	-5.6	NA	NM	NM
0.0	21.7	21.8	0.88	20.8	18.3	94	31	23.3	13.7	218	48	129
0.5	29.3	30.6	1.20	11.4	13.7	116	1	26.4	5.5	321	19	102
0.1	31.5	31.5	1.27	16.1	20.4	108	11	29.1	18.4	218	-24	127
1.5	-4.4	-3.2	-0.17	14.7	-2.4	102	-3	-3.1	NM	90	-35	174
0.3	21.1	21.6	0.89	17.3	15.4	101	11	21.4	11.1	260	12	114
0.9	23.6	23.6	0.93	17.6	16.3	115	5	20.6	12.4	186	3	137
0.6	24.7	24.5	0.84	20.5	17.2	129	9	19.0	14.7	218	31	128
1.0	21.1	21.2	0.88	13.3	11.7	95	11	22.3	15.6	231	16	121
0.3	17.1	17.2	0.73	12.4	9.1	95	4	18.1	3.1	238	4	120
6.5	-189.4	-189.1	-7.40	83.6	NM	68	-24	NM	NM	2	-92	182
0.4	17.1	17.7	0.98	13.7	13.4	105	16	16.8	82.4	NA	NM	NM
0.2	26.4	26.6	1.20	12.4	14.9	93	7	28.5	10.6	318	47	103
0.5	27.1	27.1	1.25	14.9	18.6	121	16	22.4	28.8	249	46	117
0.5	19.0	19.3	0.95	15.6	14.8	78	7	24.6	38.0	185	0	138
0.3	18.1	18.0	0.79	12.8	10.1	96	10	18.7	8.9	169	31	141

BANKS C

ASSETS

DEPOSITS

LOANS

		12/31/88 \$ MIL.	12/31/88 \$ MIL.	CHANGE FROM 1987 %	INTEREST/ NONINT. %	FOR- EIGN %	12/31/88 \$ MIL.	CHANGE FROM 1987 %	
151	UST	Boston	2332	1720	7	80/20	3	1832	19
152	MIDWEST FINANCIAL GROUP	Peoria	2325	1978	13	78/22	0	1440	14
153	FIRSTIER	Omaha	2308	1863	12	73/27	0	1332	5
154	AMOSKEAG BANK SHARES	Manchester, N. H.	2277	1679	16	90/10	0	1802	12
155	BANKS OF MID-AMERICA	Oklahoma City	2269	1818	-9	64/36	1	1024	-20
156	LINCOLN FINANCIAL	Fort Wayne, Ind.	2244	1822	12	83/17	0	1398	16
157	BANCOKLAHOMA	Tulsa	2233	1938	-7	79/21	0	1354	-15
158	UNITED CAROLINA BANCSHARES	Whiteville, N. C.	2230	2014	11	82/18	0	1514	7
159	WASHINGTON BANCORP.	Washington, D. C.	2158	1708	3	84/16	10	1586	11
160	CONSTELLATION BANCORP	Elizabeth, N. J.	2142	1831	7	72/28	0	1453	10
161	MAGNA GROUP	Belleville, Ill.	2099	1828	11	85/15	0	1296	14
162	KEY CENTURION BANCSHARES	Charleston, W. Va.	2076	1703	1	85/15	0	1065	4
163	STATEWIDE BANCORP	Toms River, N. J.	2040	1661	2	83/17	0	1369	8
164	CB&T BANCSHARES	Columbus, Ga.	1957	1674	11	79/21	0	1322	14
165	PROVIDENT BANCORP	Cincinnati	1956	1528	22	79/21	0	1309	24
166	FIRST MIDWEST BANCORP	Naperville, Ill.	1931	1666	15	83/17	0	1147	36
167	BANK SHARES	Minneapolis	1872	1482	8	81/19	0	1102	21
168	LANDMARK BANCSHARES	St. Louis	1850	1639	22	85/15	0	1340	22
169	OLD NATIONAL BANCORP.	Evansville, Ind.	1835	1481	3	84/16	0	986	7
170	MARK TWAIN BANCSHARES	St. Louis	1835	1636	8	84/16	0	1309	7
171	WORTHEN BANKING	Little Rock	1796	1578	0	84/16	0	1183	-1
172	CITIZENS BANCORP	Riverdale, Md.	1774	1443	2	68/32	0	1101	19
173	ONE VALLEY BANCORP WEST VIRGINIA	Charleston	1728	1479	12	86/14	0	1075	13
174	VALLEY NATIONAL BANCORP	Clifton, N. J.	1704	1494	11	81/19	0	1157	22
175	ASSOCIATED BANC-CORP	Green Bay, Wis.	1674	1336	6	80/20	0	979	12
176	TRUSTCOMPANY BANCORP	Jersey City	1656	1513	15	81/19	0	965	2
177	FIRST ILLINOIS	Evanston	1635	1225	8	81/19	0	1114	14
178	GRENADA SUNBURST SYSTEM	Grenada, Miss.	1633	1415	26	83/17	0	900	25
179	MITSUI MANUFACTURING BANK	Los Angeles	1608	1447	1	63/37	0	1118	-4
180	NORTH FORK BANCORP (i)	Mattituck, N. Y.	1608	1302	107	88/12	0	1154	102
181	NATIONAL COMMERCE BANCORP	Memphis	1596	1274	17	79/21	0	896	12
182	NEW HAMPSHIRE SAVINGS BANK	Concord	1581	1185	10	95/5	0	1284	13
183	FIRST INTERSTATE	Sheboygan, Wis.	1535	1282	4	83/17	0	1004	8
184	NESB (i)	New London, Conn.	1508	960	67	97/3	0	1239	81
185	FIRST COMMERCIAL	Little Rock	1493	1326	16	75/25	0	822	11
186	OHIO BANCORP	Youngstown	1484	1253	3	85/15	0	807	13
187	FORT WAYNE NATIONAL	Fort Wayne, Ind.	1474	1167	5	81/19	0	750	13
188	BOULEVARD BANCORP	Chicago	1406	1221	20	79/21	0	1031	16
189	CENTRAL JERSEY BANCORP.	Freehold	1392	1190	15	79/21	0	1017	17
190	JEFFERSON BANCSHARES	Charlottesville, Va.	1347	1191	9	84/16	0	746	13
191	FULTON FINANCIAL	Lancaster, Pa.	1337	1149	9	85/15	0	853	13
192	VICTORIA BANCSHARES	Victoria, Tex.	1328	1099	-6	79/21	0	425	-17
193	COMMONWEALTH BANCSHARES	Williamsport, Pa.	1325	1089	6	86/14	0	874	10
194	BANCORP OF MISSISSIPPI	Tupelo	1296	1145	8	83/17	0	844	12
195	CNB BANCSHARES	Evansville, Ind.	1287	1043	5	85/15	0	719	6
196	WESTAMERICA BANCORP.	San Rafael, Calif.	1274	1122	0	82/18	0	875	-8
197	HAWKEYE BANCORP.	Des Moines	1240	1088	2	87/13	0	622	11
198	FIRST NATIONAL BANCORP	Gainesville, Ga.	1213	1037	9	86/14	0	745	14
199	AMERIBANC	St. Joseph, Mo.	1154	1014	2	88/12	0	667	-1
200	CHEMICAL FINANCIAL	Midland, Mich.	1128	979	1	87/13	0	478	1

ALL-BANK COMPOSITE (Dollar figures in billions)

2322.7

1667.5

7**

79/21

17

1495.7

8**

E B O A R D

PERFORMANCE										MARKET VALUE		
NET CHARGE-OFFS AS % OF LOANS	OPER. INCOME 1988 \$ MIL.	NET INCOME 1988 \$ MIL.	RETURN ON ASSETS 1988 %	LEVERAGE 1988	RETURN ON EQUITY 1988 %	NET INTEREST INCOME 1988 \$ MIL.	CHANGE FROM 1987 %	NET INCOME AS % OF NET INT. INCOME	5-YEAR AVER. GROWTH EPS %	3/11/89 \$ MIL.	CHANGE FROM 1988 %	RANK
0.4	26.4	28.3	1.27	17.6	22.3	100	7	28.4	23.5	242	-10	118
0.4	16.3	16.2	0.73	15.5	11.3	92	10	17.6	10.2	194	67	135
0.9	26.9	19.1	0.91	12.9	11.7	82	5	23.3	4.3	196	7	134
0.3	12.4	14.0	0.67	13.7	9.2	76	5	18.4	-28.9	141	-18	151
4.6	-21.2	-22.0	-1.01	37.2	-37.5	57	-22	-38.6	NM	87	625	175
0.3	18.3	18.3	0.90	14.7	13.3	74	6	24.7	20.3	161	17	147
3.5	-73.8	-74.2	-3.50	34.5	NM	63	-22	NM	NM	5	-58	181
0.3	23.0	22.9	1.09	13.9	15.1	100	6	22.9	8.0	190	-1	136
0.9	12.9	13.1	0.62	21.9	13.6	73	14	18.1	8.1	123	18	163
0.3	21.0	21.4	1.07	17.8	19.1	88	9	24.4	15.4	222	25	124
0.6	16.7	16.8	0.85	13.8	11.7	82	6	20.5	5.6	169	4	142
0.6	23.1	22.8	1.13	9.5	10.7	87	2	26.2	4.5	265	-24	113
0.1	20.6	20.8	0.98	14.5	14.2	85	-1	24.4	6.6	167	-16	145
0.5	26.9	26.8	1.48	11.9	17.6	94	4	28.6	17.1	361	-4	95
0.1	15.9	16.2	0.94	16.0	15.0	62	19	26.2	28.2	203	26	133
0.3	15.9	15.1	0.88	14.4	12.7	76	19	20.0	16.9	205	68	131
0.2	11.1	10.9	0.62	14.7	9.1	58	17	18.8	7.2	NM*	NM	NM
0.3	12.0	12.0	0.70	17.9	12.5	66	23	18.2	1.6	97	43	171
0.2	18.7	18.7	1.08	11.6	12.5	66	5	28.4	5.7	NA	NM	NM
0.3	14.3g	14.3	0.83	19.9	16.5	73	16	19.5	9.5	154	9	148
1.5	11.2	10.4	0.59	20.2	12.0	63	4	16.4	NA	97	24	172
0.1	32.0	32.0	1.71	8.9	15.2	77	1	41.8	8.4	318	NM	104
0.5	14.4	14.6	0.91	12.7	11.5	69	6	21.2	11.3	114	-23	165
0.1	31.7	32.3	2.04	10.7	21.7	79	0	40.7	14.7	324	-7	100
0.3	14.5	15.1	0.94	15.2	14.4	62	8	24.3	12.6	134	6	155
0.6a	17.2	17.1	0.99a	15.1a	14.9a	63	11	27.2	22.8	127	32	160
0.8	29.2	29.2	1.91	11.7	22.4	85	10	34.2	31.5	416	41	84
0.5	12.2	12.3	0.81	13.6	11.0	61	9	20.1	10.0	113	NM	167
1.5	3.1	3.3	0.20	26.8	5.5	67	2	4.8	NA	NM*	NM	NM
0.1	14.3	14.7	0.91	11.9	10.9	48	33	30.4	16.1	169	NM	143
0.5	20.5	20.5	1.40	13.9	19.5	67	9	30.6	19.0	240	NM	119
0.4	3.0	3.2	0.21	15.6	3.2	48	14	6.6	NA	NA	NM	NM
0.3	12.8	13.2	0.83	12.4	10.3	64	2	20.5	5.4	128	10	159
0.3	6.5	7.8	0.66	8.6	5.6	40	37	19.3	NA	78	NM	176
0.6	13.3	13.3	1.02	13.3	13.5	56	5	23.9	10.2	128	NM	158
0.4	15.1	15.2	1.06	12.9	13.7	56	1	26.9	8.4	113	4	166
0.1	15.0	15.0	1.06	13.5	14.3	45	-1	33.1	15.5	136	-4	154
0.2	12.2	12.3	1.00	14.2	14.3	56	6	22.1	13.0	129	NM	157
0.1	18.3	18.3	1.40	12.1	17.0	58	2	31.8	12.2	181	NM	139
0.1	14.8	14.8	1.17	11.4	13.3	51	1	29.1	7.5	124	NM	162
0.1	16.4	17.8	1.40	11.8	16.6	57	3	31.1	15.4	168	NM	144
2.6	-10.9	-10.5	-0.77	13.3	-10.2	42	-7	-24.8	NM	47	-36	177
0.2	9.4	10.1	0.79	13.4	10.5	46	4	22.1	2.5	103	NM	168
0.3	13.8	12.8	0.99	15.8	15.7	55	5	23.1	14.4	103	NM	170
0.3	12.7	13.0	1.09	11.5	12.5	44	2	29.7	11.0	137	NM	153
0.9	4.8	4.8	0.38	20.1	7.6	56	1	8.5	-0.9	95	NM	173
0.1	12.2	12.2	1.01	42.3	42.8	43	3	28.2	NA	31	NM	179
0.3	20.2	16.5	1.43	11.6	16.5	52	10	31.6	15.4	176	NM	140
0.9	3.5	2.9	0.25	16.3	4.1	36	1	7.9	-29.8	41	NM	178
0.1	9.1	9.1	0.82	13.5	11.0	37	12	24.4	3.9	103	NM	169
0.9	19.2	18.9	0.83	19.0	15.7	80.8	9	23.4	10.1	140.6	14	

AGRICULTURE

THE WORLD'S CUPBOARD IS EMPTYING OUT

Lagging food production may bring disastrous shortages



DRY KANSAS FARM:
A GLEAM OUTLOOK
FOR WINTER WHEAT

The recent contamination of food by lethal chemicals caused millions of Americans to eye what's on their plates with great alarm. But what Kansas farmer Ed Johannsen sees each morning in his fields is even more frightening. The soil is so parched that he has to use a shovel to dig up the wheat powder in his hands. After a dry, cold winter the 52-year-old Little River farmer expects to lose up to 50% of his winter wheat crop. Even if rains douse the fields in the next few weeks, the US could lose about 10% of this important crop. If not, 20% will be destroyed.

It's a loss the world can't easily afford. Last year droughts and other weather calamities crippled harvests in the U.S., Canada, the Soviet Union, and Argentina. So now worldwide grain stores are at their lowest levels since the early 1970s. When the harvest starts this year, grain reserves are expected to be enough to feed the world's citizens for only 54 days. "World food supplies are at a crucial turning point," declares Edouard Saoma, director of the U.N. Food & Agriculture Organization. "More bad weather could completely deplete supplies and cause a food crisis."

FAMINE WATCH. Indeed, to many experts the real peril to food isn't safety but food shortages developing over the next several decades. "What we're seeing worldwide is a loss of momentum in food output," says Lester R. Brown, president of the Worldwatch Institute in Washington, which has just completed an analysis of world food supplies.

Brown and others argue that the Green Revolution, which produced historic rises in food production, is over. Meanwhile, environmental factors—including losses of precious topsoil and lack of fresh water—are emerging as powerful constraints on agriculture. Farmers are struggling to feed a ballooning population. "With good weather we'll be all right in the short term," but in the long run, production is not growing fast enough, says Peter Newhouse, a food expert with the FAO in Rome.

Even before the drought there were signs of slipping food production. During the mid-1980s grain production in India, Indonesia, Mexico, and China lagged. And shortages caused Africa, Asia, and Latin America to increase imports between 1980 and 1988. For the past two years, worldwide production of grain fell short of demand. Since 1981 it has dropped 9.5% from a peak of 180 million metric tons. Making up the two-year shortfall has required dipping into reserves, which have plummeted 5% since 1986, to an estimated 250 million metric tons.

Last year, U.S. grain production fell

...e, failing to meet demand for the first time since records have been kept. The U.S., which supplies 40% of the world's corn and 15% of its wheat, met export demand by selling its reserves. By May, U.S. wheat reserves will have nose-dived to 533 million bushels, down from 800 million in 1987 and well below the 800 million bushels the Agriculture Dept. considers a safe margin.

American farmers will try to make up the shortfall by planting 12% more acres this year, much of it corn, wheat, and soybeans. They will also set aside 50% more acres under government commodity programs. Some experts even predict

that the world harvest of cereals might recover. This winter heavy snows in the Northwest, the northern Great Plains, and the Rockies dropped much needed moisture. In February the Agriculture Dept. predicted that another serious drought year is unlikely.

POCKETS OF DROUGHT. But farmers from Kansas to Kazakhstan may still have good reason to be apprehensive. "We're not over this drought yet," says climatologist Cliff Harris in Chico, Calif., who makes long-range forecasts for business. Harris and other meteorologists predict large pockets of drought in North America's breadbasket. Russia is

expected to suffer one of its hottest, driest summers ever, which could cause harvests to plunge as much as 50% below normal in some areas.

Even if the heavens unleash a season of normal rainfall, "the chance of completely erasing the drought is remote," says Gail Martell, a climatologist for Shearson Lehman Hutton Inc. That's because the moisture that is normally held in the soil is depleted. In the U.S., soil-moisture levels are below normal in 31% of the cultivated land.

Crop shortages have pushed up food prices. Since last year's drought the price of U.S. wheat has leaped from

Commentary/by Naomi Freundlich

WHY THE GREAT GRAPE SCARE MISSED THE POINT

Cyanide-tainted grapes. Alar-treated apples. Pesticide-laden chicken. Corn contaminated with aflatoxins. Fish awash with poisons. Suddenly, it looks as if America's horn of plenty is spewing witches' brew.

The agencies responsible for maintaining the safety of the food supply—the Food & Drug Administration and the Agriculture Dept.—insist that what we eat is more healthful than ever. But a recent rash of news reports has environmentalists and consumer advocates wondering. "The government still lacks the basic tools to regulate effectively," charges Dan Howell, project director of Americans for Safe Food, a Washington-based advocacy group.

REAL BODIES. Yet some critics warn that the brouhaha over chemical contamination ignores a far more serious—and deadly—problem: food tainted by dangerous microorganisms such as salmonella and listeria. "You can't protect any bodies from pesticide residues," says Sanford A. Miller, dean of the Graduate School of Biomedical Sciences at the University of Texas and former director of the FDA's Center for Food Safety. "I can show you real bodies from microbial contamination."

In 1985, for example, salmonella-contaminated milk from a dairy near Chicago caused an estimated 200,000 cases of food poisoning—and at least two deaths. The problem is worsening. In 1976, 22,900 cases of salmonella infection were reported; by 1987, the number had risen to 44,609. And experts report only 1 in 40 or 50 cases is reported. The federal Centers for Disease Control estimate that 500 people die from salmonella poisoning each year.

Yet, in the face of public pressure, the FDA is planning to hire more inspectors to test for pesticide residues



NO ALAR: BUYING APPLES IN NEW YORK

in fruits and vegetables. And it has already been cutting back its microbial inspections. So Miller and others worry that microorganisms will be overlooked in the rush to ferret out man-made poisons. "The public has to recognize what the costs of this debate are," says Joseph H. Hotchkiss, an associate professor at Cornell University's Institute of Food Science. "There's no evidence that more analysis will help."

More testing might help catch the occasional apple laced with high levels of pesticides, but the jury is still out on how dangerous many of the 300 pesticides used on crops are. Except for extreme cases, the concerns with chemical residues are long-term. And Congress is pressuring the Environmental Protection Agency, which tests pesticides for safety before they can be

marketed, to speed up its reviews and long-term toxicology tests.

The problem with pesticides, says Charles Benbrook, executive director of the Board of Agriculture at the National Academy of Sciences, is that "the risks faced by the public are not evenly distributed throughout the population." That kind of uncertainty was highlighted in a recent report by the Natural Resources Defense Council.

KIDS AT RISK. The environmental group estimated that 6,000 children will get cancer sometime in their lives as a result of eight carcinogenic pesticides commonly used on fruits and vegetables. The NRDC concluded that the EPA's safe levels—which are aimed at reducing risk to one in 1 million—do not take into consideration that children eat far more fruit than adults.

It's reasonable for environmentalists and consumers to demand tough, enforceable bans on several pesticides already considered hazardous, especially to vulnerable populations. Daminozide, the active chemical in Alar, is one of them. But they also want tighter inspection of foodstuffs at the farm and market levels. Unfortunately, the FDA's field-operations budget is only \$160 million, and the agency has just 910 persons in its ranks of drug, food, and blood-bank inspectors.

Public outcry is already putting pressure on growers to limit the use of certain pesticides. It is also causing a boom in organic farming. But sending more inspectors to pick through grapes and cherries while deadly microorganisms lurk in dairy products and meat is like using the army to catch speeders while enemies infiltrate our borders. Overburdening hard-pressed inspectors to calm the public's changing fears will not keep the food supply safe.

Science & Technology

\$2.75 a bushel to \$4.65 a bushel in March. Such increases helped the federal government keep a lid on farm program costs. Last year the government paid out about \$14 billion, down from \$16.7 billion in 1987. But any prolonged period of poor harvests that pushes up the prices major producers charge for exported grain spells disaster for poor nations. Indeed, the drain of paying for imported grain would have prevented Ethiopia and Mozambique from recovering from recent droughts, even without war raging in both nations.

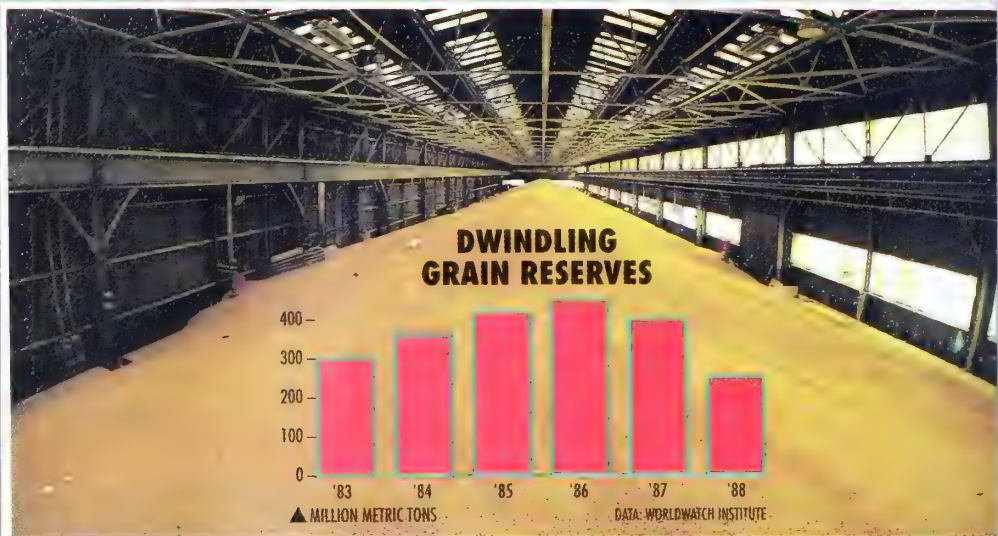
MODERN MIRACLE. But not everyone shares a grave concern about food supplies. Economists at the Agriculture Dept. point out that despite pockets of shortage and famine, the rise of agricultural productivity over the past 30 years has been a modern miracle. During the Green Revolution scientists developed hybrid strains of rice, corn, and wheat that, combined with liberal doses of fertilizers, herbicides, and pesti-

cides, caused crop yields to skyrocket. The wheat harvest in India tripled between 1965 and 1983. U.S. corn yields doubled between 1950 and 1985.

Moreover, the high prices brought on by the present drought are likely to encourage greater production. Countries such as Brazil and Argentina have millions of acres of land that could go under the plow. In the Soviet Union, the

return of some land to private farming has already helped boost production. The U.S. could increase production by bringing back 20 million acres left fallow last year under commodity programs designed to keep crop prices stable. Finally, there is biotechnology, with its promise of new strains of crops that resist drought, disease, and pests.

But future leaps in productivity from



mology are far less likely. "There's breakthrough in sight, and we've not used up the potential of the Green Revolution," says Randolph Barker, professor of agricultural economics at Cornell University. In fact, researchers have been able to significantly push up yields of rice since the 1960s. Further productivity gains from the use of chemicals will also be only incremental, concedes Will D. Carpenter, vice-president of technology at Monsanto Agricultural. And even biotechnology is not likely to produce "the dramatic revolution we saw in the early '60s and '70s," says W. H. Coffman, chairman of Cornell's plant-breeding department.

OUTJACKET. The land itself may impose the most draconian limits of all. "We're bumping up against environmental constraints," says the Worldwatch Institute's Brown. Intensive modern farming practices inflict considerable damage and can't be sustained indefinitely. Some recent gains in production come partly from planting fragile, marginal lands. Add to that a frightening loss of topsoil—some 25 billion tons each year. The U.S. has a five-year program to convert some highly erodible farmland to grass or woodland. Since 1977, the Soviet Union, with no such program, has lost 13% of its grain acreage to erosion.

In addition, supplies of fresh water are dwindling. World cropland under irrigation has almost tripled since 1950, to 645 million acres. In the process it's drawing down water supplies in several countries. In the U.S., some 25% of irrigated farmland is watered by depleting ground water. Irrigation has been principally responsible for shrinking the Soviet Union's Aral Sea by 40% since 1960.

The pressures of development and settlement continue to consume good farm-

'There's no breakthrough in sight, and we've about used up the potential of the Green Revolution'

land around the globe. Putting new land under cultivation by burning down forests in Brazil or draining coastal wetlands is shortsighted, since that irreparably destroys essential global food and forest resources.

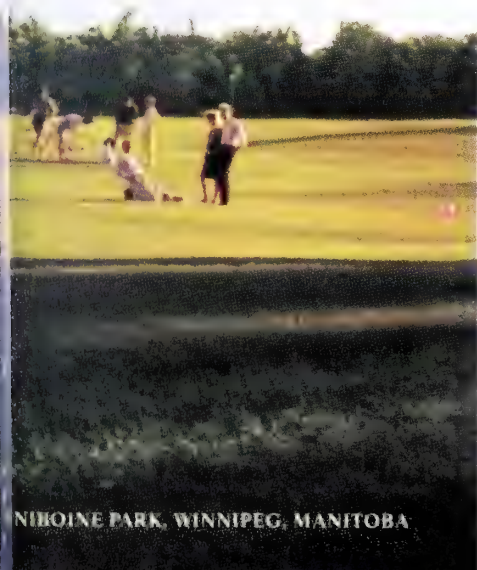
The weather may not help, either. Just as historical records show that drought cycles end, they also show periods of unusually severe drought. And those

usually occur when solar activity reaches its maximum—which is now the case. Today many climatologists and weather forecasters, using computer models of weather patterns, predict a drought as severe as that of the 1930s Dust Bowl sometime in the 1990s.

Then there's a wild card: the global warming known as the greenhouse effect. Scientists still aren't certain how such a warming, which is caused in large part by burning fossil fuels, would affect weather or agriculture. Indeed, some plants grow better in the carbon-dioxide-rich atmosphere of the greenhouse. But searing droughts and raging storms are also possibilities.

True, scientists' predictions of global famine seem to follow the same cycles as the weather. Since Thomas Malthus raised the specter in 1778, doomsayers have periodically warned that relentless growth in population would outstrip the ability of the world to feed itself. If the weather loosens its grip, concern over food supplies will again wane. But ultimately, most scientists agree, there is a limit that will be reached. And it will determine how many people—meek or otherwise—finally inherit the earth.

By Emily Smith in New York, with Lois Therrien in Chicago, Earnest Britton in Washington, and bureau reports



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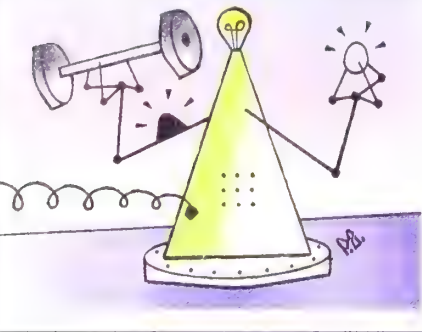
The World Next Door



Developments to Watch

EDITED BY WILLIAM D. MARBACH

THIS STEEL-COLLAR SEAMSTRESS HAS A VELVET TOUCH



Most robots do not look anything similar to the walking, talking androids of *Star Wars* fame. They are typically one-arm mechanisms that resemble a small crane. But a new robot developed by Japan's Matsushita Electric Industrial Co. has two arms, two vid-

eo-camera "eyes" to provide three-dimensional vision, and a delicate sense of touch.

The robot's first job will be on automated sewing lines in a clothing factory-of-the-future that Japan's Ministry of International Trade & Industry hopes will be operating in the mid-1990s. That means the steel-collar seamstress must gently handle limp fabrics, a tough task for any robot, while feeding them to cutting and sewing machines. The robot has an advanced 32-bit chip as a central controller and vision processor, plus smaller chips that oversee the movements of each arm and the force it uses in grasping. Matsushita says the robot's vision system and intelligence will enable it to work in "unstructured" situations ordinary robots can't handle.

CHIPS THAT SELF-DESTRUCT IF THEY FALL INTO ENEMY HANDS

The hush-hush National Security Agency, which specializes in electronic eavesdropping and sophisticated cryptography, has long engineered its top-secret equipment around custom chips with classified circuit designs. Now, to be doubly sure its most secret circuit designs don't fall into the wrong hands, NSA will make them at its heavily guarded Fort Meade (Md.) headquarters. The agency will use electron-beam technology, so it can scribe circuits directly onto small batches of chips. Late last year the electrospeaks awarded National Semiconductor Corp. an \$85 million contract to set up the chipmaking job shop.

For triple safety, the chips will be shielded by special self-destructing coatings developed by Lawrence Livermore and Sandia national laboratories. "If a hostile agent tries to take off the lid," says John D. Shea of Shea Technology Group Inc., a Saratoga (Calif.) consultant, "the coating literally rips out the top [circuit] layer."

CAN VACUUM CLEANERS HELP CLEAN UP THE PESTICIDE MESS?

After scares over tainted Chilean grapes and Alar-laced apples, food stores are scrambling to meet demand for pesticide-free produce. Usually, that means produce grown with special planting and crop management techniques. But markets in St. Louis, New York, and San Francisco are now slapping a new label on their lettuce to lure chemical-wary consumers: "Salad Vac." That stands for a novel approach to bug-control: vacuum cleaners.

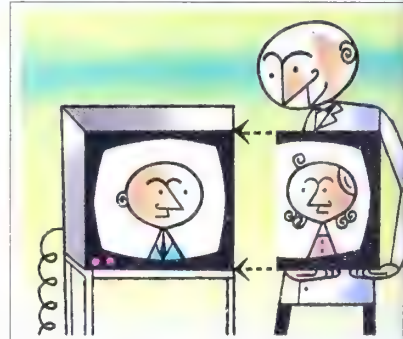
After three years of experimenting, the nation's second largest lettuce producer, Tanimura & Antle in Salinas, Cal., is using giant vacuum cleaners to lift bugs off plants in fields. The grower began its first shipments of 100% vacuum lettuce in mid-March. Unlike chemical baths, says Bob Anderson, vacuum cleaners don't stunt the plant growth. The company is spending \$5 million to develop 40 Salad Vac field cleaners for its 20,000-acre operation.

GEOMETRY COULD GIVE HDTV SIGNALS THE RIGHT SHAPE

The wide-screen, supercrisp pictures promised by high-definition TV require much more information than ordinary telecasts carry. Trying to squeeze an HDTV signal into existing broadcast channels, as the Federal Communications Commission has mandated, is giving many researchers grief. But mathematicians Michael F. Barnsley and Alan D. Sloan at Georgia Institute of Technology may have a solution: fractal geometry.

Fractals are those seemingly haphazard lines that turn out to have a strange kind of order. They are helping scientists gain insights into patterns hidden within meandering shapes such as coastlines and mountaintops. Barnsley and Sloan say the esoteric formulas can be used to encode an image and squeeze it to a mere 1/1000 of its original size.

They believe the approach offers a way to compress a signal for transmission, then reverse the process in the TV set. Barnsley hopes to develop a system by yearend. Meanwhile, the duo's Atlanta-based startup, Iterated Systems Inc., in February started marketing a \$32,500 software package for creating models of biological systems from fractals.



THAT'S NO COW —THAT'S A DRUG FACTORY

The high-tech pharmaceutical factory of the future may have four legs and a tail. Genetic engineers hope to slip new genes into cows, mice, and other animals to enable these so-called transgenic animals to produce large amounts of useful substances—such as blood-clotting factors—in their milk. Now a new report by the Congressional Office of Technology Assessment confirms that at least five patents covering such genetic engineering feats are pending at the U.S. Patent Office. Although the U.S. does not disclose such information, the OTA's researchers drew their conclusions by finding applications in Europe, where patents are published 18 months after filing.

According to the OTA, scientists at Immunex Corp. in Seattle and Pharmaceutical Proteins Ltd. in Britain are laying claim to techniques of inserting genes into the ova of large animals. And researchers at Baylor College of Medicine in Houston and Integrated Genetics Inc. in Framingham, Mass., are seeking patents not only for gene-splicing methods but for the animals that make drug-spiked milk. "Relatively small herds of transgenic animals could be used to produce significant supplies of human pharmaceuticals," the OTA report concludes.



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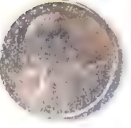
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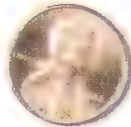
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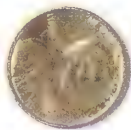
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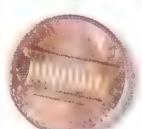
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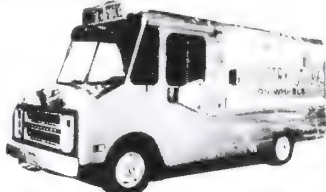
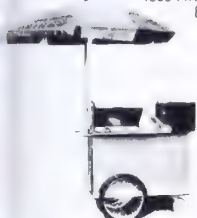
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work TV. A highly-successful
real estate broker, Freeman
owned some apartments in
her hometown of Joliet, Ill.
About 8 years ago, she heard
about Property Valuation
Consultants, a company that
lowered real estate taxes. PVC did the
job and saved her thousands of dollars
for which it received a percentage of
the savings.

Several years later, she was ap-
proached by PVC to offer their services
to her property-owning clients. Repre-
senting the company one morning each
week, she netted better than \$60,000 in
just 90 days! Freeman soon bought
PVC, and the 15-year old company is
now embarking on a major program
setting up PVC affiliates in all 50
states.

One of the best kept secrets is that
property owners can actually appeal
their real estate assessments. Nation-
ally, fewer than 2% of all assessments
are ever challenged. But a recent study
of 10 major cities shows that 4 out of 5
assessments were reduced on appeal.
"Most people don't even know how to
attempt it," says Freeman, "and we
handle everything for them in a win-win
situation."

According to Freeman, "With cor-
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exception than the rule, the
market for PVC is wide
open." Using a copyrighted
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gency basis, receiving from 1/3
to 1/2 of the savings. Most cli-
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how an incredible residual in-
come can be built up.

PVC affiliates pay a
\$9,900 start-up fee which includes com-
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else needed to get started. Ongoing
consulting is also included; PVC and its
staff work closely with each affiliate
walking them through the various steps
involved in working with clients.

"This business can be run out of a
small office or even a home," says Free-
man. "All you need is a phone. We show
our trainees how to attract as many
qualified clients as they can handle,"
she adds. "Just 50 clients per year can
net over \$100,000, and we serve more
than 1,500 clients in any given year here
in Joliet, a city of only 73,000 people."

PVC has hired motion picture and
television actor Eddie Albert as its na-
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RULE NO. 1 FOR SELLING YOUR COMPANY: DON'T RUSH

It's the stuff of an entrepreneur's dreams: the big payoff that transforms years of sweat equity into cold hard cash. But successfully running a business doesn't necessarily translate into successfully selling it. Arriving at the difficult decision to cash out is just the beginning. Preparing the company you've built for its future sale requires an exit strategy set up years in advance.

That gives sellers ample time to explore a basic but thorny question: What is your company worth in today's market? Unfortunately, there is no handy formula that will neatly calculate a business' value. Nevertheless, an old-fashioned way to gauge a private concern's worth is to look at the price-earnings ratio of comparable public companies. For a wide range of businesses and prices, check out the quarterly editions of Philadelphia-based *Mergers & Acquisitions* magazine. Their data base summarizes the terms of deals over \$1 million.

TAX RACKETS. Most private transactions are based on a multiple of cash flow (operating earnings before interest and taxes, with depreciation added back), says Chet Borgida, director of capital markets for accounting and management consulting firm Grant Thornton. "If a company has a stable cash flow and a good track record, a rule of thumb is four to six times pretax cash flow," he says. After he acquaints clients with various methods of pricing, Borgida runs the numbers through computer-pricing models. "But the way we find out what it's really worth is by seeing what the market will pay," he says.

To position your company

to get the best possible price, owners should "invest in taxes" for a few years, suggests Arthur Rosenbloom, chairman of MMG Patricof & Co., an international investment-banking firm in New York. Closely held companies are notorious for reducing the profit shown on the books so they pay less taxes. Rosenbloom reasons that if you show more profit and pay the tax on it today, you'll be more than compensated for it when you sell.

You may also want to invest in a few years of audited financials. "They're like 'a Good Housekeeping Seal of Approval,'" says Borgida. Housekeeping might also mean getting rid of any outstanding lawsuits that might alarm a buyer. More important is grooming a successor, especially if you want to exit the company soon after you sell it.

Some sellers decide to go it alone when selling, while others call in a deal adviser. Minneapolis businesswoman Anne Kerr sold her real estate-marketing service without using a deal adviser, but with help from her longtime certified public accountant and lawyer. Kerr used a multiple of earnings to determine her price and then ran the numbers by her CPA.

But selling your business can be as time-consuming as running it. "It's difficult to sell your business and still do your job," says John Sturm, who used Grant Thornton to sell a 12-year-old business that designs and manufac-

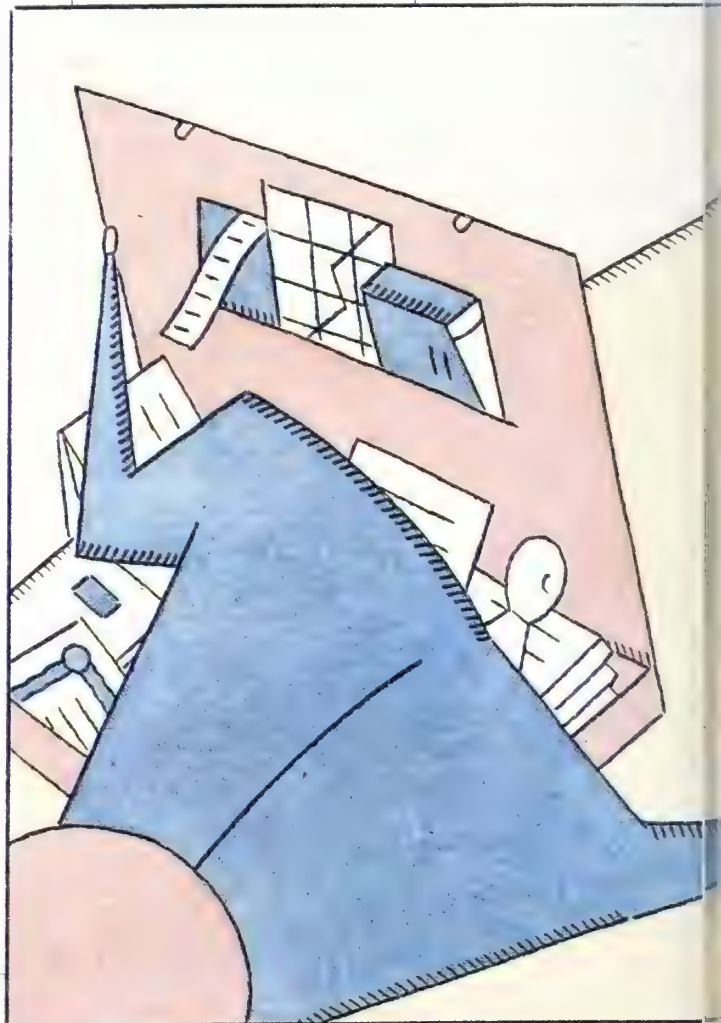
tures exhibits for trade shows. The personal chemistry between you and your adviser can be important as a deal wears on: Sturm conferred with his adviser every other day for the year it took to complete his sale.

BROKER BASICS. The type of adviser you'll add to your team depends largely on the estimated purchase price of your company. If it is going to sell for a few million dollars or less, you will probably want to turn to a business broker. "The best way to find a broker is to talk to other buyers and sellers," says Lisa

Berger, one of the authors of *Cashing In: Getting the Most When You Sell Your Business* (Warner Books, \$19.95).

Business brokers operate much like real estate brokers. They're paid on commission for deals under \$500,000, could be 10% to 12% of the purchase price. When the price hits a million, the percentage shrinks, say, to 5%. If the price is between one and two million, you may pay 3% and so on.

Most brokers aren't regulated by any agency, so check references and make sure a broker has expertise selling



type of company. An experienced, qualified broker will work out well, but inept brokers may price a company of the market or below its value. It's also possible that an inexperienced broker will breach a confidentiality agreement when shopping your company around. So, before you sign any agreement with a broker, run it by a law-experienced in selling businesses. It's a good idea to get advice from lawyers and accountants whose fees aren't contingent on the sale of your business.

SUCCESS FEES. If your company's price tag is between \$1 million and \$100 million, you may want to use a region-investment banking firm or middle-market division of one of the larger investment-banking or accounting firms. For a deal with a purchase price of \$20 million, Shearson Lehman Hutton would ask for a retainer of about \$50,000 to \$100,000, to be subtracted from

PREPARING FOR A SALE

1 Don't relax your day-to-day operations in preparation for—or in the midst of—a sale. If anything, push to generate even higher profits to entice buyers with your growth potential.

2 Pull out assets that may not be fully compensated for, such as real estate that you could lease back to the buyer.

the final "success fee," which could amount to around \$550,000. Success fees can be about 5% of the purchase price, estimates Arnold Hoffman, director of Shearson Lehman Hutton's Philadelphia-based middle-market group.

Deal advisers will want to make sure that you're not just testing the waters to see what the market will bear.

3 Consider an environmental audit to reassure buyers that your company has no potentially costly pollution-related problems.

4 Have potential buyers sign nondisclosure agreements to protect against leaks to employees and clients.

5 If your lease is coming up for renewal, check with your landlord so you can tell buyers the estimated rent increase. Make sure the lease is transferable.

Some firms will ask for a retainer, while others may suggest that you buy a "business valuation" from them. In-depth business valuations may be helpful in giving you a point of reference and laying out your company's strengths and weaknesses, but many people question their value. "All the information comes from the principals, and these companies charge exorbitant fees," says Kerr.

To arrive at a value, Geneva Cos., a provider of merger-and-acquisition services to middle-market businesses, recasts company financials for the past three years on a public-company basis. Their "evaluation and strategies reports" include earnings projections for the next five years, market research, and their estimate of the company's fair market value. If you use Geneva to sell your company, half of the \$29,500 cost for these reports is subtracted from their commission.

SPIKE BUYERS. Industry experts warn of a bait-and-switch approach in which potential sellers are given inflated valuations in hopes of persuading them to sell with the evaluating company. Buyers and sellers may find a valuation more credible if it is conducted by an independent third party.

Once you've come up with a price range, you need to target potential buyers. Your goal may be to find a strategic buyer, a company more interested in synergy than in bottom-line financials. These so-called spike buyers often pay premium prices.

Last fall, one strategic buyer's bid for a small life-insurance company was 25% higher than the bids of buyers who focused solely on the company's financials, says Peter Mattingly, a partner at New York investment banking firm Wassner Mattingly & Co. However, price may not be your main objective. Sturm turned away an English buyer who offered more for his exhibits company in favor of a New York buyout firm whose goals he felt were closer to his.

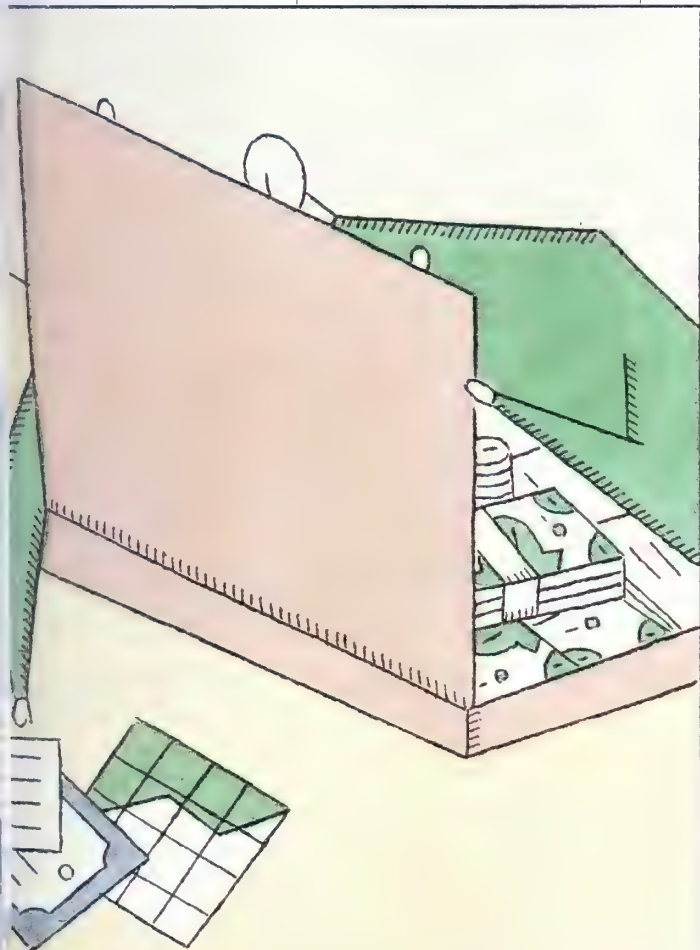
TICKET ABROAD. Another basic question to ponder is what role you want at the company after it's sold. If you want to remain and have no qualms about selling to a foreign buyer, many European and Japanese companies will pay premium prices and may offer greater autonomy. And if you think your company should expand abroad, you'll gain a valuable beachhead.

To maintain a minority interest, you could sell to a leveraged-buyout (LBO) group. "In many cases the owner in an LBO stays on with a smaller share," says Borgida. "They've cashed in, and they still run the company." But LBO groups usually pay the lowest prices.

If your goal is to sell 100% of your company and head for the tropics, you may get a lower price. Most buyers want the seller to remain, if only for a transition period of months to a year or two.

Whichever path you choose, the timing of a sale is crucial. "Most people sell on the downside. But you should sell on the upswing, when you're sitting there like a fat cat," says Thomas West, editor of *The Business Broker*, a newsletter based in Concord, Mass. Because no one wants a company whose best years are behind it.

Suzanne Woolley



Smart Money

LIKE THOSE RATES YOU SEE? THEN TAKE THE LONG VIEW

Interest rates have been hovering in the alluring 9%-plus range lately. But if you believe today's rates could quickly become a memory, the safest place to lock them in for years—or even decades—is in medium- or long-term U.S. Treasury securities.

Buying shares of bond funds is one popular choice. But since mutual funds keep buying and selling government bonds, you wouldn't be locking in a fixed rate. You can buy newly issued Treasury bonds and notes through a Federal Reserve Bank, commission-free, at periodic auctions. However, you might have to wait as long as three months for a new issue of, say, five-year notes.

Buying T-bonds from brokers means markups—so shop

If you want to nail down a rate that caught your fancy in the morning paper, you can buy existing bonds in the secondary market from a broker. There's no wait for the auction date, and you can minimize your cash outlay by buying on margin. All it takes to sell is a phone call to your broker.

LOOK AROUND. Problem is, the T-bond market is geared to professionals who make multimillion dollar trades. Since retail investors are such small fry, they will pay a high markup for their relatively small orders. But for purchases of \$100,000 or more, it pays to shop around for the best deal, says Jay Goldinger, president of Capital Insight, a small Beverly Hills brokerage.

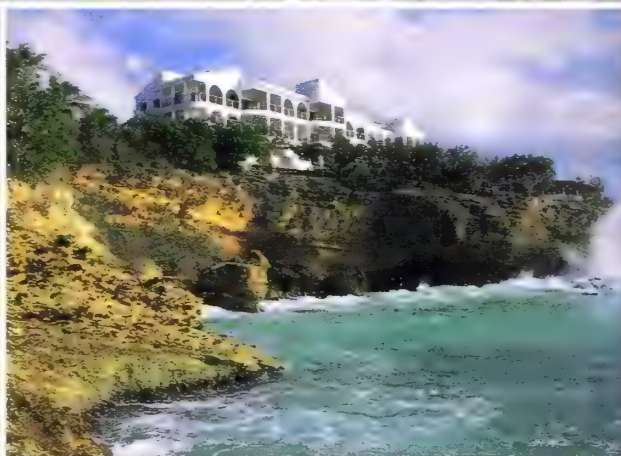
When you choose a broker, try to find one who specializes in bonds. One way to do this is to ask the brokerage branch manager to make a recommendation.

Goldinger suggests maintaining accounts with about five brokers so you can get price quotes from each. Large, full-service brokerages also are dealers in government bonds and are most likely to have a large inventory of T-bonds.

HIDDEN SPREAD. It's not always easy to tell what markup brokers are charging, because the price quote probably has the markup built into it. Here's a subtle way of figuring out what the transaction is costing you: Instead of just getting the buy price for a specific maturity, ask the broker what the price would be if you wanted to sell. The difference between the two prices is the spread, or the markup. For your \$100,000 order, \$100 would be a reasonable markup, and modest against the interest income of \$9,000 or more a year. For larger amounts, too, try to pay no more than \$1 per \$1,000, says Goldinger.

For purchases of less than \$100,000, the investor pays a much steeper markup of \$5 to \$7 per \$1,000. The broker might tell you, for instance, that you can buy a four-year note at \$980.9375 per thousand, or sell it for \$973.7500. That's a spread of \$7.1875. On \$20,000 of notes, that comes out to a markup of \$143.75.

You'll have to be an aggressive investor to pay commissions as low as \$1 per thousand. If you find you're paying much more, or aren't inclined to bargain, you're probably better off waiting to buy directly from the Federal Reserve. *Leah Nathans*



THE MALLIHOUANA: NO BEACH BASHES, JUST REFINED R&R

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HEAVEN CAN WAIT—FOR NOW, TRY ANGUILLA

These days the hottest place in the Caribbean is Anguilla. Unlike St. Martin and St. Croix, this tiny bit of the British West Indies remains sparsely populated and unspoiled. And among the Caribbean cognoscenti, the hottest place on Anguilla is the Mallihouana hotel.

When real estate developer Leon Royden was looking for a site for his resort, he chose Anguilla because "it was the quietest island I could find." It still is—partly because getting there is a bit involved. The most common route is to fly to St. Martin, then take an eight-minute plane ride or a choppy 20-minute crossing by ferry. But enroute hassles soon are forgotten upon arriving at Mallihouana: Even when all 50 rooms are full, the hotel radiates tranquility.

MEAN CUISINE. Decorated in a kind of colonial Mediterranean, the open-air lobby—adorned with stucco pillars, arcades, and archways—descends in levels toward the sea. Doors and windows throughout are trimmed with brass and dark Brazilian walnut, and the perfume of vanilla-scented candles fills the air.

"Tranquility" also characterizes the management style. Party animals, beware: There are no cocktail parties or

beach luaus or late-night entertainments. Guests may make do with two white-sand beaches, three pools, and tennis courts. For indoor recreation, try the library, television room, or exercise gym.

What makes the Mallihouana truly unusual, however, is its fine cuisine. The colonied dining room, managed by French chef Rostang, known to gourmets for his two-star restaurant on the Riviera and in New York. Most of the food, along with the staff, is imported from France to ensure production of such specialties as a crispy pasta with cauliflower or lobster risotto.

It's not too early to reserve for next winter (809 497-6100). You may have to wait for cancellation, as requests for "same room, next year" have become a tradition—and are tantamount to guests who may change rooms in midstay to accommodate the regulars.

The cost of being pampered at the Mallihouana is steep, and no credit cards are accepted. Rooms start at \$400 a night for a double and go up to \$850 for a two-bedroom suite. You might think that would include meals (easily \$20 a day). Alas, no. The best things in life aren't always free. *Troy Stal*



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Getting Ahead

HOW TO GRAB —AND HOLD— AN AUDIENCE

Such business celebrities as Steve Jobs and Lee Iacocca have a built-in advantage when they make speeches. But if your name alone isn't enough to keep a crowd hanging on every word, these tips might help:

Use slides, not a blackboard or flip charts, says Jane Ann Schiltz, who makes numerous presentations as a marketing director at Northwestern Mutual Life. "That way, I never have to turn my back, and can keep eye contact." But, she warns, "be careful not to dim the lights too much."

MIKE FRIGHT. Intimidated by microphones? "Don't use one," says Roger Flax, head of Motivational Systems in South Orange, N.J., which trains executives in communi-

cation skills. A mike isn't needed for any group smaller than 150 people: "That's just 10 or 12 rows, and your voice should carry that far." No mike means no problems with feedback or volume adjustments. And you can move freely about for emphasis.

To end worries about boring the crowd, map out exactly how much you want to say. A technique taught by T/K Training International in Vancouver, B.C., involves structuring each address in just three parts. Then you keep in mind an image of a triangle or other three-part object—mentally moving from one part to another, then quitting. "People who know a lot want to talk a lot," says T/K's Shelagh Kennett. "A disciplined structure gives you confidence."

You may destroy that confidence if you start with a joke, says Flax. If it bombs, the re-



sultant groan can unnerve you. Instead, involve the audience by opening with a rhetorical question, such as: "Which do you think you'll appreciate more: the year you're

living now or a year from now? You'll live in the future?" The question should lead into the topic, but you've got listeners think: "Am I being asked to

Make ears perk up, too, by delivering your first words in a louder-than-normal voice. Loosen up your vocal cords, sing all-out in the shower or car on the day you speak.) Any throat-clearing before you're introduced in front of the crowd shows nervousness.

Don't hold notes in your hands shake. The paper's motion magnifies it. To avoid rubbing your empty hands nervously or jamming them in your pockets, tuck your elbows against your sides and de-

ately make a gesture with your first words, says Flax. "If your presentation is as important as it should be, you'll continue to gesture naturally as you speak." Don D.

Fashion

TIES THAT LET IT ALL HANG OUT

Haberdashers have a saying: A tie is a man's flag. Judging by that sartorial standard, executives these days are flying high. Not since the 1970s have ties been so fat and sassy. Unlike those creations, the new crop is cut in the old-fashioned bottle shape—wide at both the throat and the bottom. And they emphasize rich hues and bold designs—anything from abstract florals to a geometric hodgepodge of circles and triangles.

Even conservative dressers are exchanging pin dots for polka dots. They're also trying stripes of a different color. Forget the

blues, the burgundies, the yellows. The new power shades are purple—a favorite of John Kennedy Jr.—or green, or both. Often, it's not just one color, it's unusual combinations, says Jim Eisen, men's furnishings manager of Saks Fifth Avenue. Ties selling from \$50 to \$70 by Armani or Valentino blend as many as eight different hues.

What's causing men to drape the equivalent of an expressionist painting around

their necks? The tie is about the only outlet the male executive has to be dashing, says Terry Dobris, vice-president of tie maker Format. Even in a conservative company, wearing one of these splashy cravats probably won't do you any harm: "The tie is an area of acceptable eccentricity," says designer Bill Robinson. But don't think you can drag that five-inch number from 1974 out of the closet. Dashing is one thing. Dated is another.

Troy Segal, David Castellon



Worth Noting

■ **CLUTTER CUTTER.** Herman Schlemmer's alarm clock Electronic Desk Block builds everything you need into its frame: a pushbutton phone with speaker and memory for 112 numbers; a calculator with memory; a call-timer stopwatch, and a clock-calendar with alarm (\$732; 800 543-3366).

■ **AUDIO AUDIT.** If you're called to an audit, the taxpayer Bill of Rights allows you to tape-record the proceedings. To find out other rights you have as a taxpayer, the IRS offers a booklet *Your Rights As A Taxpayer* (800 424-3676).

■ **MOVING ON.** You may usually deduct moving expenses if you move to change jobs, notes the *Arthur Young Tax Guide 1989*. And under many miscellaneous deductions, these expenses are deductible even if they don't exceed 2% of adjusted gross income.

I INFORMATION
& **I** IMAGE
M MANAGEMENT:

**HIGH-TECH
ALTERNATIVES
TO PAPER**

You may not recognize the name, but if you've ever looked up an old newspaper on microfilm at your local library, you're familiar with the early accomplishments of an industry called information and image management.

Once confined to micrographics, the industry today has merged high-tech capabilities with its long experience in document storage and retrieval.

Its latest applications are improving the speed and accuracy of business and even changing the way it is conducted.



CHARLES SMITH PHOTOGRAPHY

Scaling the Paper Mountain

Put in simplest terms, I&IM offers ways to deal with the 1.3 trillion documents currently overflowing offices across the country. A full 95% of that information is in the form of paper, a virtual mountain of computer printouts, photocopies, letters, and so on, that is said to be growing at nearly a billion new documents every day.

Managing these staggering amounts of paper is the mission of the I&IM industry. From conversion of paper into spatially efficient media for cost-effective storage and ready retrieval, to electronic manipulation of the original information and images, I&IM cuts the paper mountain down to a manageable size.

"Serious observers no longer talk about the 'paperless office,' because paper is such a good medium for displaying image-based information," says Sue Wolk, Executive Director of the Association for Information and Image Management (AIIM), headquartered in Silver Spring, Maryland. "But paper is cumbersome and

ultimately very expensive when it comes to storing, retrieving, and manipulating the information. That's where our industry comes in."

The industry is gaining a higher profile rapidly as insurance companies, airlines, manufacturers, hospitals, providers of financial services, local and state governments, even the IRS, are finding I&IM's major efficiencies impossible to resist. Workers spend less time filing and retrieving, customers are serviced more quickly and more efficiently, and accounts are processed with far fewer errors. The result is a distinct competitive advantage.



YES, EVEN PAPER COMPANIES ARE ELIMINATING PAPER FILES

They don't want their name used, but they think their story is amusing enough to share. They are a large paper company in the Northeast who distributes paper products for use by airline in-flight services, fast food chains, hotels and motels. Now to make sure that they could maintain a steady daily flow of over 8,000 different stock items, they needed a fast, efficient, and accurate records management system. So their thousands of customer account records were gradually transferred from paper to microfilm for rapid search and retrieval of vital information.

All their signature copies/invoices are now kept on line with an extensive computer-assisted-retrieval (CAR) system

from Minolta Document Imaging Systems. Within seconds any of these copies can be located on a computer index and retrieved automatically on plain paper reader-printers.

Under the old, manual paper filing system, it would sometimes take several months to find an invoice, an overwhelming job for six file clerks with over 10,000 bills of lading and other documents in 20 full file drawer cabinets.

Now with the microfilm CAR system, overtime has been completely eliminated, and the only cost in personnel for filing and filming is two persons' salary plus benefits. The other four file clerks? They're handling paper again—but products the company makes, not invoices it receives. Cost justification for the system was justified in less than a year.

Yes, even a paper company can use I&IM.



High Visibility Applications

If you have an American Express card, you've probably gotten statements with the image of your original, signed receipt slip reproduced in reduced size. That's an image management system that gives you a visual confirmation of what you spent last month.

If you called your insurance company about a claim in process, you might have been surprised when a few keyboard clicks in the background brought your handwritten letter instantly to your agent's attention. No more holding for five minutes. That's because your letter is stored in an electronic file.

Tried to cash a check at your bank and got a teller who didn't know you? Remember how that teller stepped back to a small file drawer, took out a piece of film about the size of an index card, slipped it into a machine and checked the signature on your check with a blown-up version on a screen? That film was a microfiche, the machine was a reader, and the technology is perhaps the oldest, least expensive, and most widely used in business today: micrographics.

"High visibility applications are helping the industry come into its own in terms of recognition of what it can do," maintains James Breuer, Director of Communication at AIIM. "We're getting a boost from both sides now; even without knowing the technology by name, the consumer perceives the benefits of I&IM and seeks those companies that use it. The companies themselves recognize that consumer perception as a means to a competitive advantage because added value translates into higher marketshare."



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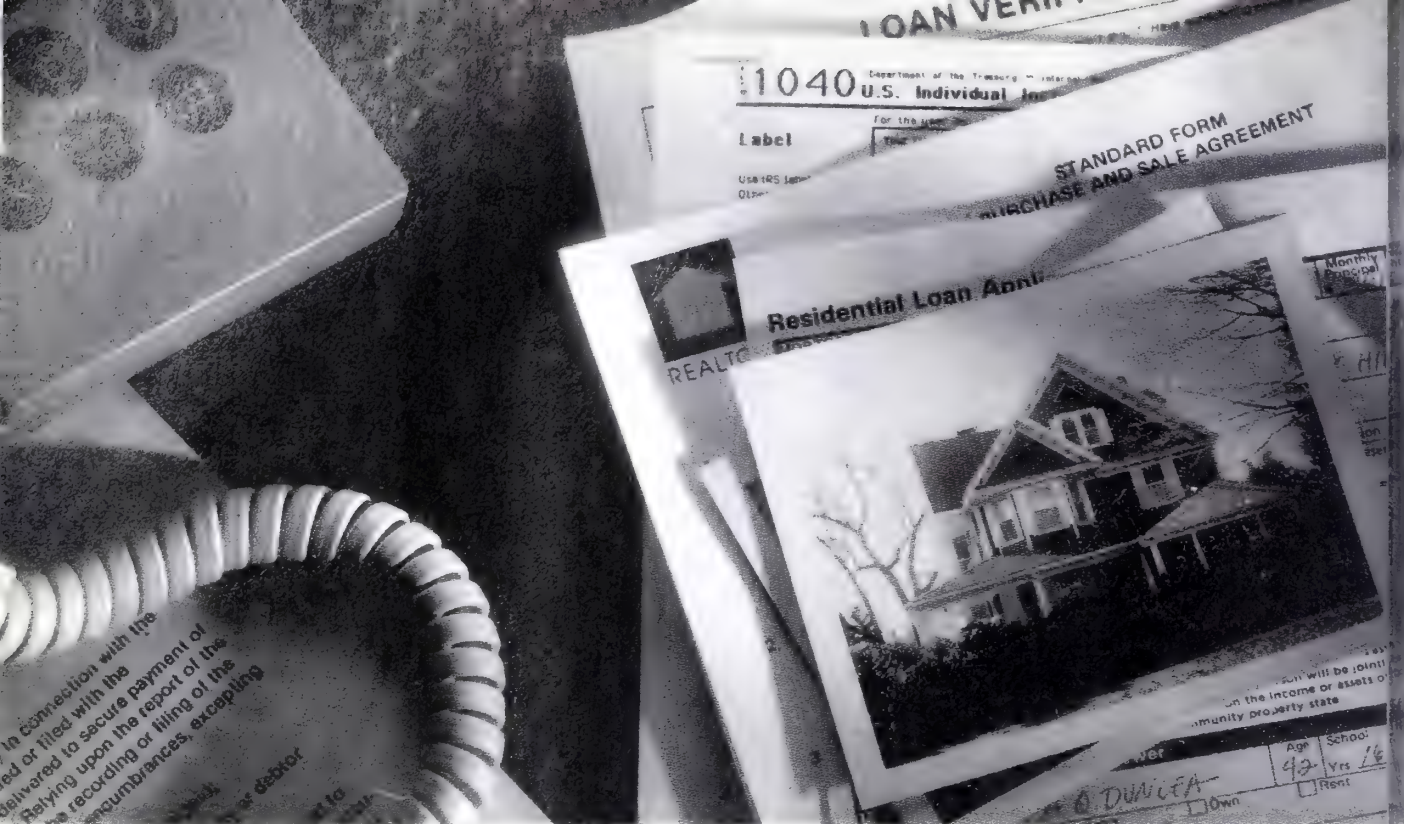
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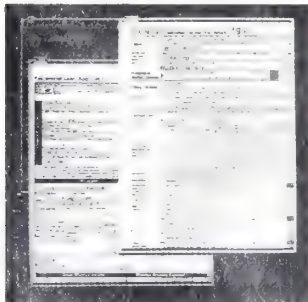
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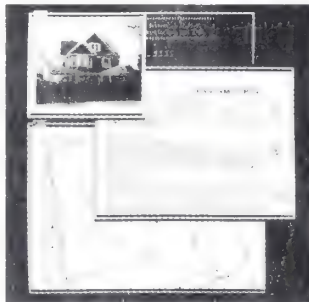
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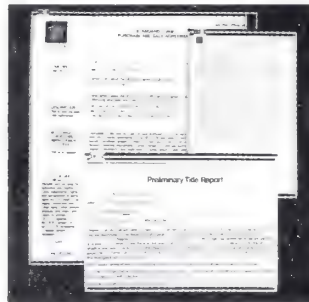
CAN A BETTER IMAGE IMPROVE CUSTOMER SERVICE? BANK ON IT.



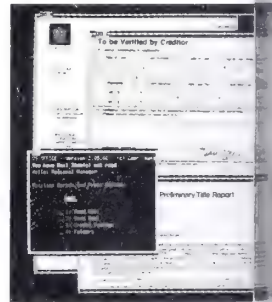
*Customer comes in for a mortgage.
Has a loan application, tax returns.*



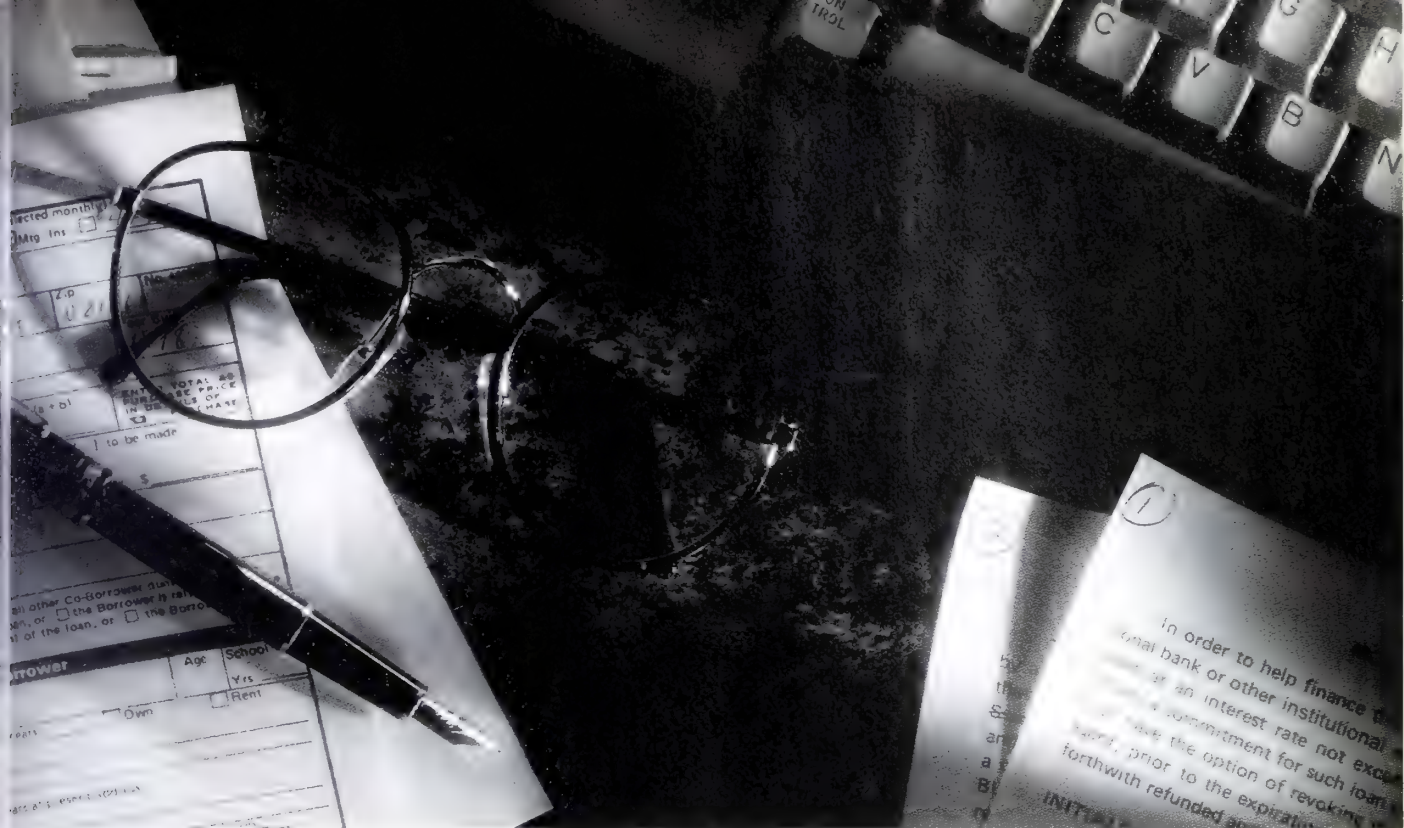
*Bank appraiser mails in photos of
property, plot plan and comparables.*



*Broker provides offer to purchase,
preliminary title report,
and P & S agreement by FAX.*



*Credit information arrives, added
to client portfolio.*



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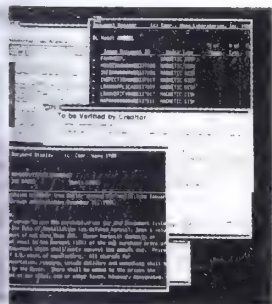
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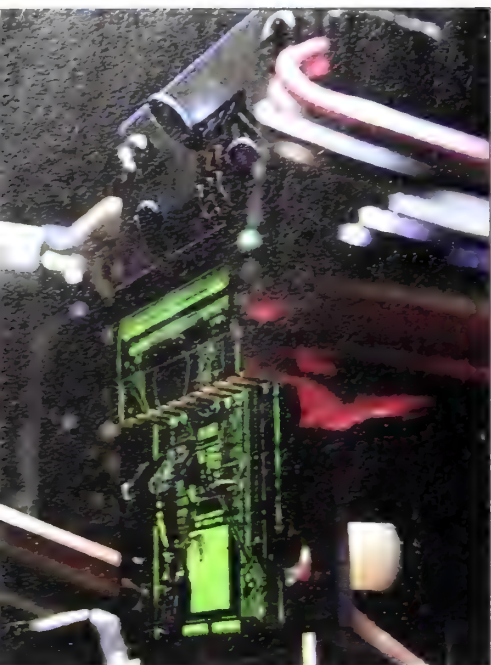
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The Technology
and the Future

New technologies, with their new jargon, acronyms, and redefinitions of old words, can intimidate the best of us. And an industry with the formidable title of Information and Image Management suggests that there's probably a lot here that mere mortals cannot understand. Not so. We can, and with ease.

All the technology can be summed up in five basic operations that are performed on the original piece of paper: 1) Input; 2) Storage; 3) Retrieval; 4) Manipulation; and 5) Output.

Think of it this way: a piece of paper arrives at your desk (input), you file it in a drawer (storage), you take it out when the need arises (retrieval), you write a note on it (manipulation), and you send it to someone else (output).

But in I&IM the paper is unnecessary once it arrives.

1. First the information and images on the paper are "captured" by a piece of equipment and **input** into the system. Four types of input devices are used for capturing:

Optical Scanners look and function like paper copiers and are used to digitize a document for input into an electronic system. They handle several hundred pages or more per hour.

Microfilm Cameras film the document and reduce its size for storage either as microfilm (rolls) or microfiche (sheets). Processing occurs in a separate darkroom or in-line with filming.

Facsimile Machines send and receive document images worldwide directly from one imaging system to another.

Optical Character Recognition OCR converts a scanned image into ASCII data, eliminating most keyboard entry.

2. The second operation, **storage**, is media dependent, meaning microform, magnetic disks, or high-speed optical disks:

Microforms are either rolls of microfilm or sheets of microfiche. A single storage and retrieval device can house as many as 300 microfilm cartridges.

Magnetic disks and magnetic tapes are familiar media used with most computer systems. They are used for storing digitized images in low-volume applications or for temporary storage.

Optical disks are high-volume write-once/read-many (WORM) devices. One 12-inch disk holds about one gigabyte of data on each side, about eighteen full-size file-cabinet drawers of documents. Data are "compressed" to allow higher density storage, that is, the white space on a page is recorded in a kind of shorthand. Optical disks can be stored in **stand-alone drives**, used in relatively low volume applications, or in **cabinet-mounted drives** which are suitable for medium-volume handling. In both, the disks must be manually inserted and flipped to access the other side. For large-volume applications, **optical jukeboxes** utilize high-speed robotics to mount and dismount as many as 150 disks through up to five separate drives. By linking multiple jukeboxes in a system, quick access to hundreds of millions of images can be achieved. Watching one of these marvels in action is like seeing

STATE MEDICAL LABORATORY SETS UP MICROGRAPHIC RETRIEVAL SYSTEM FOR PATIENT BLOODWORK HISTORIES

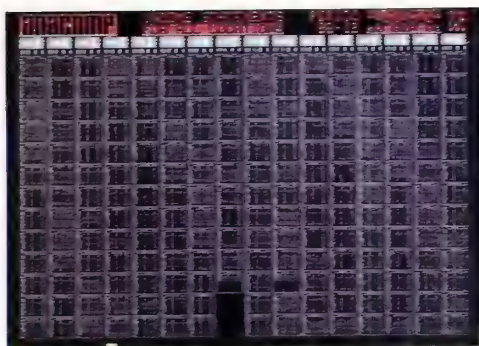
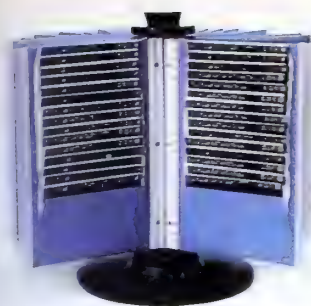
A northeastern state medical laboratory needed a way to look up past bloodwork histories easily for patients who could not remember their lab ID number. The problem was extensive because most repeat patients kept no record of their ID number.

With the help of an Anacomp software micrographics package, the laboratory set up a retrieval system that allows staff to access past histories by a number of different identifiers. These include patient name, social security number, or date. The system automatically indexes the file with cross reference microfiche at the time the file is created.

Prior to this micrographic system access to files could take up to an hour or more. In some cases, histories that were misfiled were never found. Today, however, over 40,000 tests per month, including virology, toxicology, and microbiology, are processed onto microfiche with cross referencing and made available to state lab staff mere seconds after inquiry. And the inquiry can request patient name, social security number, date, or account number.

When first looking to solve their problem, the lab managers examined on-line computer-based solutions. By comparison, the costs of the micrographics system—to accomplish the same task—were a mere fraction of the computer system.





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Wisconsin Physicians Service in Madison, Wisconsin is one of the nation's largest contractors for CHAMPUS which provides health care benefits for military retirees and dependents of active duty personnel. Serving as a CHAMPUS fiscal intermediary, WPS processes more than 2.5 million claims for CHAMPUS beneficiaries in the Mid-Atlantic and South Central Contract regions.

Through the use of 3M's Document System Division new integrated systems for microfilming and microfilm retrieval, WPS has seen claims retrieval productivity increase significantly. The automated retrieval system has improved claim request turnaround time from five days to one day, and it has reduced staff in the microfilm/files unit by 21 employees. The system paid for itself in only one year.

The staff reduction is the direct result of the increased efficiency provided by automated microfilming and retrieval operations. WPS were able to eliminate paper files altogether and now use only the microfilm to handle all claim requests.

Preprinted, bar coded ICN labels are applied to claims as they are received and after the adjusting step, all processed claims are immediately filmed and indexed.

its namesake load and unload a dozen 45's in under a few seconds.

3. The third operation, **retrieval**, is so linked to storage that much of its process has been described above. The key to rapid retrieval is **indexing**, most of which is done automatically when the document is initially stored. Microforms use "blips" and x-y coordinates, while magnetic and optical disks employ user-specified document identifiers for indexing.

Computer-Assisted-Retrieval (CAR) systems utilize computer storage of the indices to achieve rapid retrieval of document images from microform or disk storage systems. A CAR system can be thought of as the "intelligence" behind "smart storage."

4. Some, although not all, applications require some **manipulation** of the information and images, if only the addition of more information to the original document. Manipulation or examination of the document occurs at **workstations** where the image is displayed on a screen. Workstations can be **dedicated**

or can be add-on options that allow existing **PC workstations** to function as image workstations. A PC display and an image processing workstation differ in two ways: the latter has significantly higher resolution and can be twice the size of a PC screen. The double size permits multiple document viewing side-by-side.

The workstation can be **multi-purpose**, functioning as a word processor, a database access device, a transaction processor, a telecommunications device, a window to the mainframe and other workstations—the operator's link to the rest of the system.

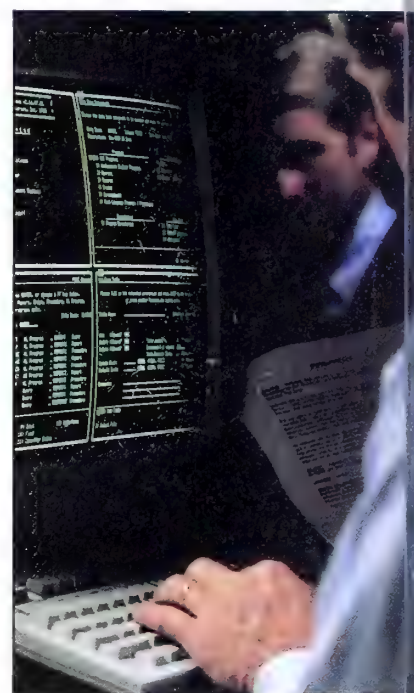
5. The final operation, **output**, is also media dependent. In a micrographic system, the microform is usually read on a stand-alone viewing device called a **reader**, which is simply a film projector with good optics. **Reader-printers** produce a hard copy of the screen image at the same size as the original. **Computer Output Microfilm (COM)** devices output the information directly onto microform.

For electronic digitized images stored on magnetic or optical media, hard copy printouts can occur through **laser printers** which have the necessary resolution to print image as well as textual information. Digitized images can also be output directly into **electronic mail** and routed anywhere in the system, and using standard telephone lines the image can be FAXed literally anywhere in the world.

AIRLINE SECURITY TIGHTENED AND AIRLINE MAINTENANCE RECORD RETRIEVAL SPEEDED UP

In the summer of 1988, the Board of Airport Commissioners for the Los Angeles International Airport (LAX) purchased an Edicon security/access control system. The Kodak image/information system allows guards to verify an employee's identity and status immediately. Employees are required to place a computer-coded photo ID badge onto a sensor device which activates a color, TV-quality image of the employee, along with verifying information. Former employees, or those without proper clearance, are denied access. The central processing station is linked to five inspection posts at key entryways.

Another Kodak digitized imaging system is being used by a large passenger airline headquartered in the South to manage their maintenance records. In addition to mainframe software records of schedules and completed procedures, paper records



Technological Choice Are Application-Drive

Newcomers to the technology insist on separating micrographic systems and electronic systems. Micrographics supporters point to its economy, stressing that it provides spatial efficiencies, longevity (centuries when stored properly), legality (long

are required by the Federal Aviation Administration (FAA) to prove a particular maintenance procedure has been performed. Electronic summaries are not acceptable to the FAA; they require copies of the original forms signed by the mechanics.

Some records audits can involve documentation of repairs over the entire life of an aircraft, and the airline has limited time to produce the data. If they can't respond readily, the FAA can impose fines of up to \$10,000 per landing, retroactive to the document's due date.

Before installing the Kodak KIMS system 5000, the airline relied on a paper filing system. Now incoming documents are immediately scanned, and index data are entered at an adjoining workstation. Images are written to optical disks within robotic library. Later, as documents are needed, the images are transmitted electronically over a local area network to workstations for display or to laser printer for hard copy, suitable for all FAA needs and requirements. Fines are a thing of the past, and maintenance records are accurate, timely, and cost-effective.



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DOCUMENT IMAGING
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accepted by the courts for evidentiary purposes), uniformity of size, and ease of use—all for a relatively small investment of capital. Electronic systems supporters argue that ultimately digitized imaging results in cost savings through the greater efficiencies in processing. For high-volume databases that require frequent and ready access, for transaction processing that demands flexibility and full file integration, for multiple-user access and distribution, they insist that electronic systems are the first choice.

In fact, they're both right. The appropriate technology is that which is best suited for the specific application. That means some users will employ both micrographics and electronic information management (EIM) in the same business for different tasks.

For example, consider the bank that stores account information on microfiche for tellers' use. That same financial institution may use EIM to speed up check processing by returning to the customer not the original check but the captured image of the check, thereby eliminating the need to pass that original piece of paper through several channels and across a number of desks. And the same system

CHARLES SMITH PHOTOGRAPHY



that prints up the monthly statement can also generate an image of the cancelled check.

I&M
in the
Corporate World

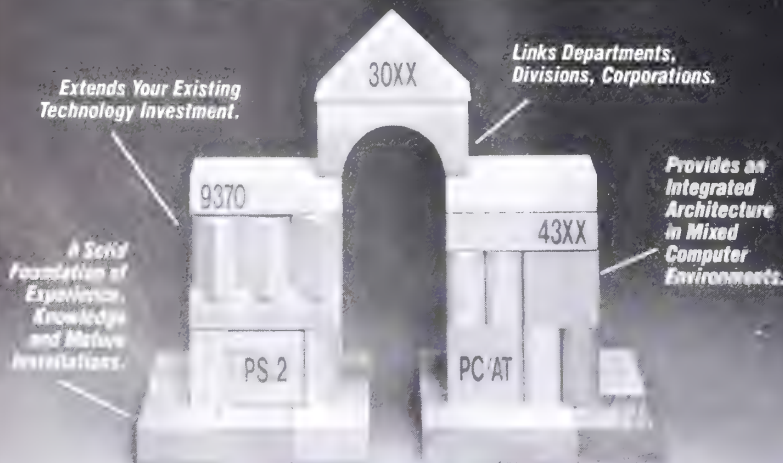
The higher the volume of document processing and storage, the greater the cost savings realized—which is why I&M has such strong appeal in the corporate world. The overall effect can be dramatic: frequently changing the organizational work is accomplished. Workers find themselves ascending rapidly up a learning curve that invariably reaches higher than planned, evolving transaction automation improvements that are more beneficial than anticipated.

A couple of years ago, initial inquiries were originating with middle management and below, that is, from the people directly involved in the day-to-day movement of work who sought I&M solutions to real problems. Today, with increasing frequency, those initial inquiries are coming from corporate-level management who see the competitive advantage I&M offers.

In a broader context, much is being made these days about information as a corporate asset. Over the course of years doing business, companies gather information, much of it in image form, that directly impacts their day-to-day operations. That information is at least as valuable as the company's plant and equipment—perhaps more so. By increasing the accessibility of information, I&M makes it possible for companies to begin managing that most valuable asset.

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The building could be replaced. But what about your company's files? Suppose you're audited by a major client. Would your Accounts Receivable department have immediate access to all the necessary files, or would it take days of sifting through old files and storage rooms?

The problem is, and always has been, paper. Paper that when misfiled or misplaced could spell disaster. Paper that when destroyed, could possibly destroy your business.

The solution is a computerized filing system from 3M Document

Systems Division.

3M provides systems that use computer technology—very likely the computers you already have in place—to speed and secure the storage and retrieval of documents with evidentiary value. Documents that can be combined with the data files you already generate on computer.

For many businesses, the storage media may be microfilm or microfiche. With certain applications, an optical recording system integrated with a mainframe database may be most appropriate.

Either way, the system you choose will work with the technology 3M is developing for the future. We've already assembled packages to help those in the areas of Accounts Payable, Engineering, Manufacturing, Financial Records, Hospital Records and more.

For more information on how to protect your company against both natural and unnatural disasters, call 1-800-328-1684, ext. 57 (in MN, 1-800-792-1072, ext. 57).

But call soon. Because like your records, even the best of intentions can go up in smoke.

3M DOCUMENT SYSTEMS DIVISION

3M

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AND DATA.
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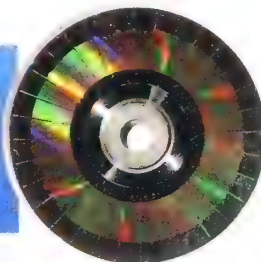
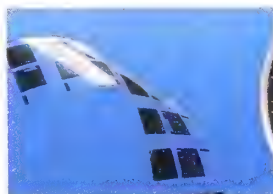
Why Kodak? For three good reasons.

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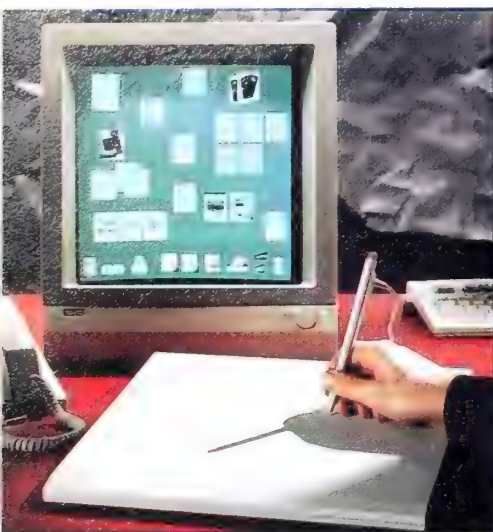
A 60-year head start. Nobody understands imaging better than Kodak. We're already supplying systems that link mainframes, optical disks, and micrographics. That's expertise you can bank on today.

Find out how we can build an image link between your people and information. Call 1-800-44KODAK, ext. 380.



The new vision of Kodak





I&IM in Small- and Medium-Sized Businesses

Prospective purchasers of I&IM technology have several options available to them that will help them decide which approach and which equipment are best suited to their needs. Foremost among these options is attendance at the 1989 AIIM Show and Conference to be held in San Francisco from June 5th to the 8th. Manufacturers and suppliers of I&IM products and services use this show as the primary avenue for reaching their most important prospects. New products and systems are routinely introduced at this event.

AIIM is also the best source for information about those companies which comprise the industry, and about the industry itself. AIIM's Resource Center is the world's most complete I&IM library, containing over 11,000 items. AIIM's annual *Sourcebook* has a compendium of products and services offered by the 350+ member companies, with all information cross-indexed.

Small- and medium-sized businesses might find their initial forays into I&IM best served by a **service bureau** or a **full-service dealer**. These suppliers will convert paper to any medium and, in some instances, will provide storage facilities as well. The large number of **dealers** in the industry sell a variety of types of equipment from a range of manufacturers, suitable for businesses seeking equipment to supplement present systems already in place.

Manufacturers of imaging systems are responding to the needs of small- and medium-sized businesses with new, innovative **low-end systems**, several of which are planned for introduction at the June show in San Francisco. These electronic infor-

NEW YORK CITY IMPROVES VOTER REGISTRATION WITH IMAGING

In New York City, too many people have had difficulty voting because their registration cards are misfiled, or the cards don't get processed and filed in time for the election, or the cards just don't make it to the right polling place on election day. Last November in Staten Island, the Board of Elections for New York City tried out an imaging system called RegiStation from Image Business Systems to address the problem.

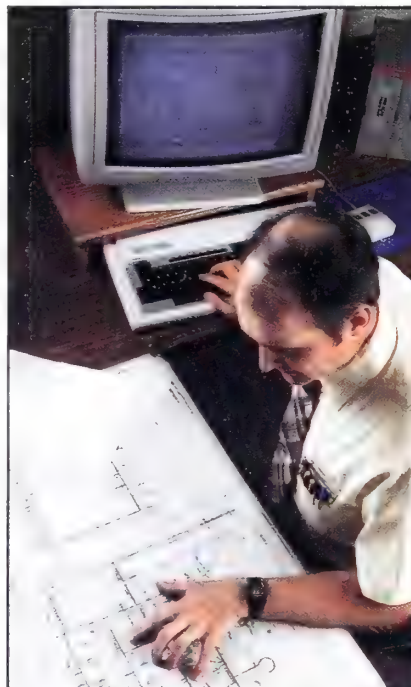
The idea behind RegiStation was to put New York's current 3 million voter registration documents into the mainframe

computer for last-minute printouts so that every polling place has up-to-date lists of registered voters. That by itself was not a new idea in the Big Apple. What was new was the inclusion of the original signature from the voter's application right on the polling place list.

The imaging system digitized the signature, stored the digitized signature in the voter data file, and made the image available for instantaneous comparison with the on-site signature.

The system's success was borne out by acceptance among precinct workers, city workers, and voters alike. New York is moving ahead to determine what it will take to install IBS's RegiStation throughout all five boroughs.

mation and image management systems include a scanner, a server (processor), a workstation, an optical disk storage device, and a laser printer. Both microform and WORM-based systems are available. Of course, the operating system software is included in all such packages.



Building an Industry on Evolutionary Migration

In 1987, I&IM industry revenues were \$2.75 billion in the U.S. alone. Forecasts for 1991 predict performance at \$4.2 billion. Industry leaders attribute the dramatic growth to one overriding fact: the industry is built on responding to customer needs.

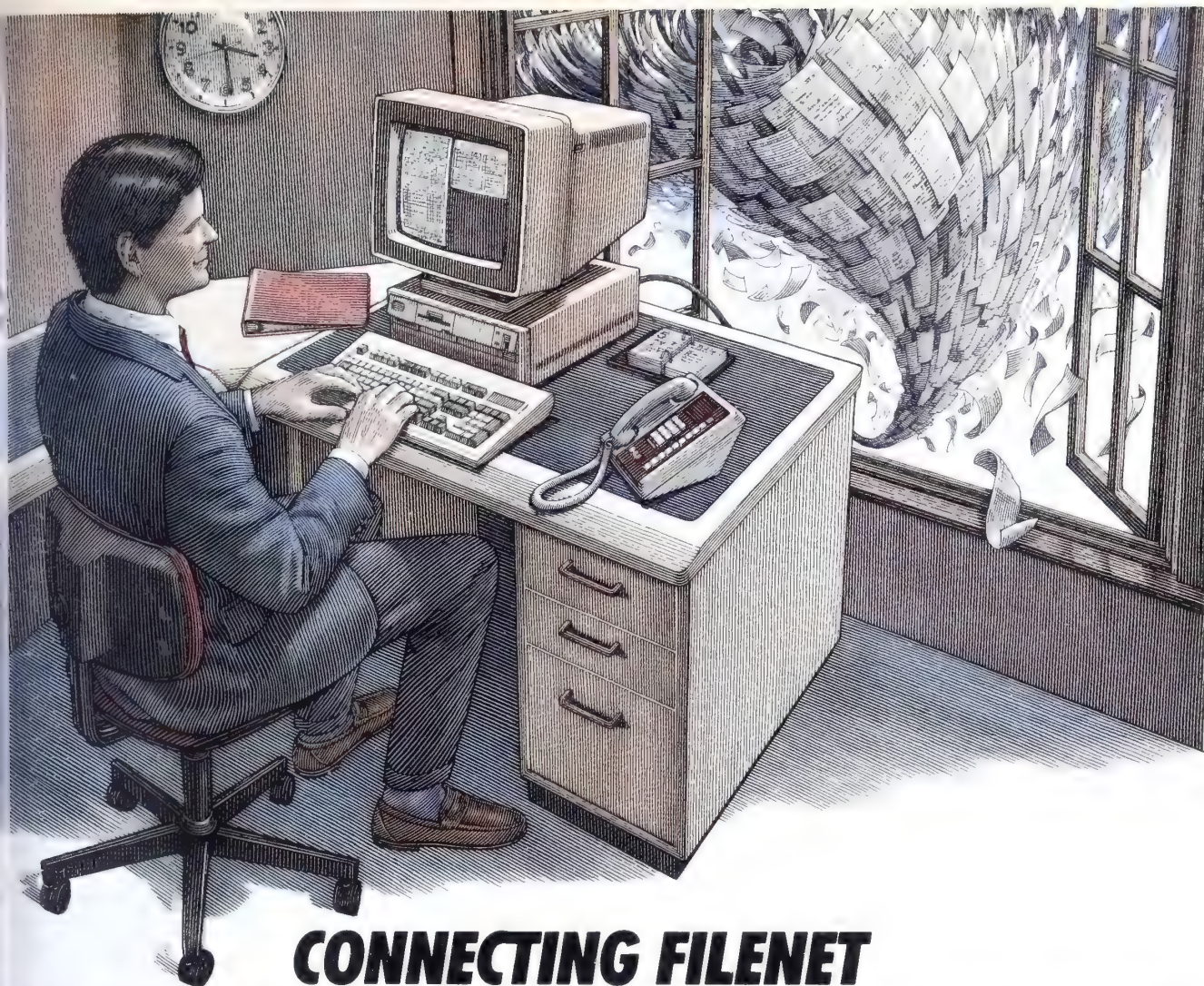
QUALITY ASSURANCE DOCUMENTATION PROCESSES STREAMLINED AT ALLIED-SIGNAL AEROSPACE COMPANY

At Allied-Signal Aerospace Company, quality assurance audit trails must accompany all of the missile and undersea components produced by the Fluid Systems Division in Tempe, Arizona, documenting where the parts originated, test results, and certification information.

To handle its paperwork demands, Allied-Signal has installed an integrated imaging system from Wang Laboratories, Inc. Documents are now scanned into the imaging system as materials enter the receiving area, and the system retrieves information directly from the division's mainframe to validate shipments received against the original purchase order.

For many of the military components built by the Fluid Systems Division, the quality assurance group produces logbooks of material certifications, assembly build and test records, and various associated documentation. A data package can have as many as 300 pages and more than 30 packages a month are produced.

"Since we no longer have to search manually for information, we can compile the materials at one-third the time it took by hand," explains Bayard Kulb, Director of Quality Assurance. "Imaging is also helping us cut down on storage space and shift personnel from manually filing and retrieving documents to more productive tasks. And by using the imaging system, we are reducing the time it takes to manually input data into the mainframe from eight hours to less than one."



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The thousands of documents flying daily in your organization represent up to 95% of your workload. Your PCs can't handle such massive amounts of paper. So the image processing is done manually—highly inefficient and mistake-prone system—while your PCs sit idle.

Now FileNet puts the incredible power and efficiency of image processing into your PC network for on-paper processing.

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FileNet image processors integrate seamlessly into your network, transforming your PCs into image workstations. So now, in addition to data and text, your PCs

can process the other 95% of work that has resisted automation. Which makes your PCs—and their operators—more productive.

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FileNet's rich, open software architecture offers benefits far beyond mere storage and retrieval. Its WorkFlo® family of application software enables you to conveniently manage the movement and use of information throughout your organization, integrating images with existing mainframe and PC applications.

And as your system grows, FileNet can link PCs from various departments into networks with hundreds of users.

No wonder organizations like

Citicorp, John Hancock and the U.S. House of Representatives have enabled FileNet to build the largest installed base of image processing systems in the world.

Get the facts today

To find out how FileNet can make *your* PCs 95% more efficient, get your free copy of *A Strategic Perspective on Integrated Image Processing* by calling:

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AMERICAN AIRLINES KEEPS TRACK OF FREQUENT FLYER MILES ON OPTICAL DISK

American Airlines AAdvantage program has millions of participants. Each day, the carrier's service center receives thousands of pieces of correspondence, including flight boarding passes used to credit mileage, car rental invoices, and personal letters from customers. In addition, service representatives respond to thousands of phone calls each day from their members.

"Customers are anxious to know if we received their request for a travel award and when they'll get it. Was their account credited for a flight or the use of one of our car rental or hotel co-ops? Are they eligible for a certain award?" explains Linda LaFever, Operations Manager for the airline's Frequent Traveler Programs.

An optical-disk, document-image processing system from FileNet brings together all the information relevant to a customer account—including correspondence and account mileage data—to help service representatives efficiently answer a range of customer questions immediately by calling up the customer's 'electronic' file on a workstation. "Instead of having to look for a file or track down a piece of correspondence, we can display the document-images as well as data from our mainframe using multiple windows on one screen," said LaFever.

All incoming documents—from the full-page letter to the flight boarding pass—are scanned and digitized as soon as they are received.

"The FileNet WorkFlo software routes the incoming correspondence to the appropriate service representative for processing.

"Document-image processing has enhanced how we manage information. The system works to eliminate the delays and inefficiencies associated with handling, storage, and retrieval of paper," said LaFever.

Satisfying the user has taken on greater meaning and urgency as competition in I&IM heats up. In the early 80s, when new storage and communication technologies were first being introduced, the capabilities of the technologies themselves attracted potential users. Today, however, actual users are demanding solutions tailored to the requirements of their specific situation. That demand is not lost on suppliers, who are working more closely than ever to provide not just technologies, but solutions to customer needs.

Within the user organization, five dis-



tinct groups are becoming involved in identifying the need: senior management, micrographics or records management, MIS, technologies assessment groups, and—ultimately—the user's customer. So many groups are involved because the solution often has enterprise-wide implications, that is, it impacts not just a single individual or even department, but the entire organization.

These are some of the preliminary observations made by the market research firm of Temple, Barker, and Sloane, recently commissioned by AIIM to perform the first empirical study of the I&IM industry. The study, which will be presented at the June show, will contain a full-blown assessment of the size, trends, and direction of the industry.

Hand in hand with I&IM's enterprise-wide approach is its commitment to evolutionary migration of the technologies. The tacit rule throughout the industry is: if it can't be done with equipment already in place at the user's business—at *any* user's business—then don't produce it.

"We don't have standards set for all aspects of the technology," explains Marilyn Courtot, Director of Standards and Technology at AIIM, "but we are working continually toward that end. In the meantime, our manufacturers are doing their best to make their products adaptable to what's already out there."

Evolutionary migration means that, when a business incorporates I&IM technology, image processing comes in as an add-on, a facilitator to what already exists. Some view that fact alone as a technological breakthrough.

Personal Imaging in the 1990s

Where, you may ask, is this technology taking us? Looking back, we can see mainframes in the sixties, word processing in the seventies, the personal computer in the eighties. Is imaging, the next logical step in the evolution of high technology, to be the industry that characterizes the nineties? Will there be an imaging system in every home by the year 2000?

Analysts are arguing that so much has happened in the past five years that it's impossible to predict where the industry will be headed by the mid nineties. A general sense prevails that there will be fewer islands of technology, thanks to more extensive software applications. Full integration of text, data, image and voice is expected.

What seems most certain today is that increasing numbers of businesses will incorporate the current capabilities of I&IM into their operations automation, if for no other reason than to keep up with their competitors who already have.

This Special Advertising Section was sponsored by the Association for Information and Image Management. For more information, please contact: AIIM, 1100 Wayne Avenue, Suite 1100, Silver Spring, MD 20910. Tel: 301-587-8202, Fax: 301-587-2711

The text was written by Ronald J. Bognore in conjunction with USA Chicago, Inc.

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ADVERTISEMENT

Small Company's New Golf Ball Flies Too Far; Could Obsolete Many Golf Courses

Pro Hits 400-Yard Tee Shots During Test Round

Want To Shoot An Eagle or Two?

By Mike Henson

MERIDEN, CT — A small golf company in Connecticut has created a new, super ball that flies like a #2, putts with the steady roll of a cue ball and bites green on approach shots like a dropped cat. But don't look for it on weekend TV. Long-hitting pros would make a joke out of some of golf's finest courses with it. One pro who tested the ball drove it 400 yards, finishing the green on all but the longest par-fours. Scientific tests by an independent lab using a hitting machine prove the ball out-distances all major brands dramatically.

The ball's extraordinary distance comes partly from an evolutionary new dimple design that keeps the ball 1 ft longer. But there's also a secret change in the core that makes it rise faster off the clubhead. Another change reduces air drag. The result is a ball that gains altitude quickly, then sails like a glider. None of the changes is noticeable in the ball itself.

Despite this extraordinary performance the company has a problem. A spokesman put it this way: "If you need endorsements and TV publicity. This is at gets you in the pro shops and stores where 95% of all golf products are sold. Unless the pros use you on TV, you're virtually locked out of these outlets.

TV advertising is too expensive to buy on your own, at least for us.

"Now, you've seen how far this ball can fly. Can you imagine a pro using it on TV and eagle-ing par-fours? It would turn the course into a par-three, and real men don't play par-three's. This new fly-power forces us to sell it without relying on pros or pro-shops. One way is to sell it direct from our plant. That way we can keep the name printed on the ball a secret that only a buyer would know. There's more to golf than tournaments, you know."

The company guarantees a golfer a prompt refund if the new ball doesn't cut five to ten strokes off his or her average score. Simply return the balls — new or used — to the address below. "No one else would dare do that," boasted the company's director.

If you would like an eagle or two, here's your best chance yet. Write your name and address and "Code Name S" (the ball's R&D name) on a piece of paper and send it along with a check (or your credit card number and expiration date) to National Golf Center (Dept. H-1044), 500 S. Broad St., Meriden, CT 06450. Or phone 203-238-2712, 8-8 Eastern time. No P.O. boxes, all shipments are UPS. One dozen "S" balls cost \$21.95 (plus \$2.50 shipping & handling), two to five dozen are only \$19.50 each, six dozen are only \$99.00. You save \$47.70 ordering six. Shipping is free on two or more dozen. Specify white or Hi-Vision yellow.

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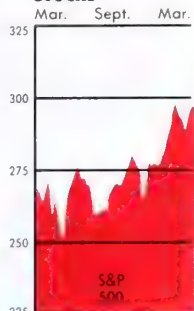
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Investment Figures of the Week

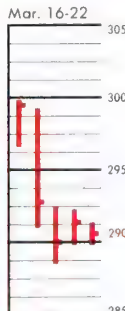
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, but at midweek smaller-
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ked off a strong rally in

STOCKS

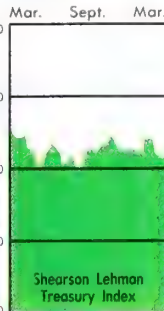


52-week change
+8.0%

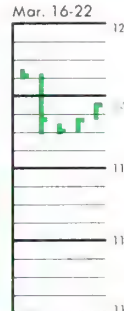


52-week change
-4.7%

BONDS

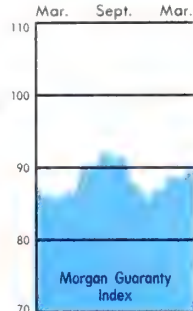


52-week change
-4.7%

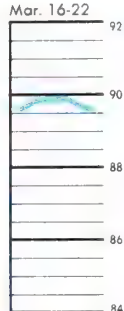


52-week change
+3.3%

THE DOLLAR



52-week change
+3.3%



52-week change
+3.3%

MARKET ANALYSIS

STOCKS	Latest	% change Week	% change 52-week
ONES INDUSTRIALS	2263.2	-2.5	9.5
MPANIES (Russell 1000)	153.6	-2.0	7.8
COMPANIES (Russell 2000)	156.0	-1.5	9.0
MPANIES (Russell 3000)	165.1	-2.0	7.9

FIN STOCKS	Latest	% change Week	% change 52-week
N (FINANCIAL TIMES 100)	2048.6	-3.4	11.8
N (NIKKEI INDEX)	31,443.2	-2.0	21.4
TO (TSE COMPOSITE)	3558.0	-1.8	5.9

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	9.0%	8.7%	5.8%
30-YEAR TREASURY BOND YIELD	9.2%	9.1%	8.8%
S&P 500 DIVIDEND YIELD	3.6%	3.4%	3.4%
S&P 500 PRICE/EARNINGS RATIO	11.7	11.9	15.5

TECHNICAL INDICATORS

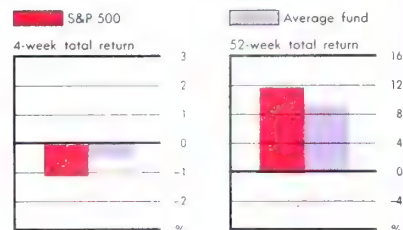
	Latest	Week ago	Reading
S&P 500 26-week moving average	281.6	280.7	Positive
Stocks above 26-week moving average	56.6%	63.0%	Neutral
Speculative sentiment: Put/call ratio	0.30	0.26	Neutral
Insider sentiment: Vickers sell/buy ratio	1.12	1.11	Positive

INDUSTRY GROUPS

WEEK LEADERS	% change 4-week	% change 52-week	Strongest stock in group	% change 4-week	% change 52-week	Price
S	7.4	-28.1	REEBOK	12.6	-10.8	14½
STAINMENT	5.8	24.9	WARNER COMMUNICATIONS	14.9	46.4	48½
GAS DRILLING	5.4	-11.8	HELMERICH & PAYNE	10.4	-1.0	25½
ITAL MANAGEMENT	4.9	24.5	HUMANA	11.2	11.2	28½
ESTIC OIL	4.2	1.7	AMERADA HESS	9.1	20.4	36½
WEEK LAGGARDS	% change 4-week	% change 52-week	Weakest stock in group	% change 4-week	% change 52-week	Price
EBUILDING	-22.7	-7.5	KAUFMAN & BROAD	-27.8	13.7	10¾
REIGHT	-12.5	7.9	FEDERAL EXPRESS	-13.3	4.0	45½
PUTER SYSTEMS	-10.6	-7.0	INTERGRAPH	-32.2	-47.0	15¼
CONDUCTORS	-10.0	-23.9	MOTOROLA	-11.4	-17.1	39¾
UMENTATION	-9.9	-11.3	HEWLETT-PACKARD	-10.4	-13.1	53¾

MUTUAL FUNDS

RS	%	LAGGARDS	%
ek total return	%	Four-week total return	%
ATEGIC INVESTMENTS	18.2	STRATEGIC GOLD/MINERALS	-12.9
ED SERVICES GOLD SHARES	17.4	ALLIANCE TECHNOLOGY	-7.3
RNATIONAL INVESTORS	7.1	MERRILL LYNCH PACIFIC	-7.3
k total return	%	52-week total return	%
FMANN	56.8	STEADMAN OCEANOGRAPHIC TECHNOLOGY	-22.7
ITY STRATEGIES	34.3	STRATEGIC INVESTMENTS	-19.2
JMBIA SPECIAL	32.4	FIDELITY SELECT ELECTRONICS	-16.8



RELATIVE PORTFOLIOS

amounts ent the present of \$10,000 ed one year each portfolio	Foreign stocks	U. S. stocks	Money market fund	Treasury bonds	Gold
ages indicate total returns	\$12,010 -1.52%	\$11,129 -1.29%	\$10,653 +0.16%	\$10,084 -1.74%	\$8,869 -0.57%

on this page are as of market close Wednesday, Mar. 22, 1989, unless otherwise indicated
groups include S&P 500 companies only; performance and share prices are as of market close

Mar. 21. Mutual fund returns are as of Mar. 17. Relative portfolios are valued as of Mar. 21. A more
detailed explanation of this page is available on request

INFLATION: BUSH NEEDS TO FLEX SOME MUSCLE

The faster pace of producer and consumer prices tells us that we have now entered a new inflationary cycle. During the 12 months ended in February, inflation in producer prices accelerated to 5.4%, from 1.8% during the previous year. And consumer price inflation picked up to 4.8%, from 3.9%. Even more important, the bond markets and investors overseas are telling us that we are on the brink of a revival of inflationary expectations. Inflationary expectations are extremely dangerous. When they are fanned, policy has to get ever tighter to cool things down.

In the Ronald Reagan years, people here and abroad were so convinced of the anti-inflationary fervor of the Administration that they believed, come what might, inflation could not regain a toehold. That's one reason why the U.S. is in the longest peacetime expansion in history. The markets are now telling us that this faith in Washington's resolve no longer holds true. We have a new Administration that has yet to establish the anti-inflationary credibility of its predecessor. Barely three weeks after Inauguration Day, Bush made a mistake when he warned Federal Reserve Chairman Alan Greenspan not to choke the economy. He also sent Congress a budget full of bookkeeping tricks.

These early moves are leading to worries about the nature of the Fed's anti-inflation role. When interest rates rose last week, it was because the markets were responding to the new producer-price index figures rather than to nudging by the Fed. In other words, the Fed is seen as reacting to events rather than creating them in the anti-inflation battle.

Reports from abroad suggest that in addition to the domestic bond market's worries, the Europeans—who have their own inflationary pressures to worry about—are not convinced of the Bush Administration's resolve to dampen inflationary expectations. Such doubts are often self-fulfilling. Until now they have not been reflected in the value of the dollar in the foreign-exchange markets, which has been comparatively stable. But unless President Bush and his troops quickly show their anti-inflationary colors, this is a battle that could disintegrate into a rout. Bush must now provide strong leadership on getting the budget gap closed and pledge the Fed his full and unreserved backing in its anti-inflationary fight.

SALINAS DESERVES A SHOW OF SUPPORT

In his first 100 days, Mexico's young President, Carlos Salinas de Gortari, has come on like gangbusters. He has attacked foes, from corrupt union bosses to insider-trader types, with swift blows and has worked quickly to put Mexico on a painful, if necessary, modernization regimen. His gutsy resolve has already gained respect from leaders around the world.

Washington has reason to welcome Salinas' determination as well. On some of the issues that chafe Mexico-U.S. relations, Salinas has shown much flexibility. He has devoted more resources than his predecessors to fighting drug trafficking, which he says "carries a national security risk to the Mexican state." The U.S. Senate should keep that in mind when it votes to certify Mexico for continued aid in its battle against drugs. And U.S. trade officials, long frustrated by Mexican trade barriers, should be pleased with Salinas' commitment to keep Mexico a member in good standing among General Agreement on Tariffs & Trade nations.

Still, there are some troubling aspects of the Salinas administration. His early displays of power may have generated headlines, but they also showed a leader perhaps a bit too ready to pull the trigger. In his confrontations with an increasingly restive rank and file, Salinas is in danger of alienating a populace with many legitimate demands. Indeed, despite demands from many Mexicans, Salinas seems to be busier consolidating power than expanding democracy.

Salinas is the man Mexicans and Americans have to deal with. He has already proved a forceful leader. Let's help him get his country on firm economic footing now and iron out differences later.

SOME FOGGY IDEAS MAR THIS CLEAN-AIR PLAN

Los Angeles buildings fade into the smog, and a bluish cloud hovers over the freeways. Last year, the four-county area exceeded one federal air-quality standard 199 times, the most in the nation. Often the city was three times as dirty as allowed by law. No wonder L.A.'s area pollution-control board and local government were overwhelmed on Mar. 17 for a sweeping plan to clean the region's air by the year 2007.

There are plenty of measures in the Los Angeles plan that, while onerous, make sense. In lawn-obsessed Southern California, the plan's ban on gasoline-powered lawn mowers is reasonable, as is a proscription against charcoal-grill oil or fluids in the land of the barbecue. Spray deodorant is banned, and all auto tires will have to be radials in order to reduce the rubber laid down on city streets by Angelinos.

Longer-term proposals in the plan are another matter. Within 19 years, for example, 40% of all cars would have to burn methanol or run on electricity. No one knows whether either of these technologies would be remotely feasible, indeed, whether they would even be more environmentally benign. Where would the electricity come from? Coal-burning plants? Nuclear reactors? Where would we get methanol? From strip-mined coal?

Paradoxically, it was the Environmental Protection Agency that forced L.A. to act after looking the other way during the Reagan years. Other cities, which could have similar problems, will be closely watching as the plan balances business concerns with a vital need to clean the air. It must establish standards and set stiff penalties for violating them. But those standards should not specify favored technologies or force anyone to use methanol or electricity.

April 10

WIN A NATIONAL LOTTERY IN YOUR FUTURE

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PAGE 26

BusinessWeek

APRIL 10, 1989

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MASTERS OF INNOVATION

How 3M Keeps New Products Coming

PAGE 58

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Over at the Chair Plant in Grand Rapids they're still talking about Wayne Meuser, the night-shift foreman, and his assistant, Terry VandenAkker. Still shaking their heads and smiling.

Just the other night, the production crew got into a jam because their chrome vendor was having trouble getting a clean layer of chrome down on the T-line chair frames. Vendor tried everything, even sent over extras, trying to make schedule.

But around 3:00 AM, as they were welding and buffing out the last of the shipment and flecks of chrome started flying off, it got to be pretty clear that things weren't going to work out right. The night shift was going to come up a few frames short. Wayne will tell you: "Steelcase is real picky about quality. They want to make sure

the customer is getting top of the line for his dollar."

Well sir, two frames short, they got lucky. Talked a security guard into unlocking Quality Control. As a last resort. They found four masters. Took the best two, left the tags and a note—"Thanks, we needed these for schedule!"

Next day, QC wasn't too happy. The plant superintendent even told them that if they ever pulled a stunt like that again, he'd think about giving them some unpaid vacation. But, as Terry put it, "in the end he figured it would be a lot easier to replace the master frames than it would be to replace the customer, if the full order wasn't received."

Understand, Steelcase has this motto: "The schedule must be met at all costs!"

All those boys did was take it literally.

Stunt men.



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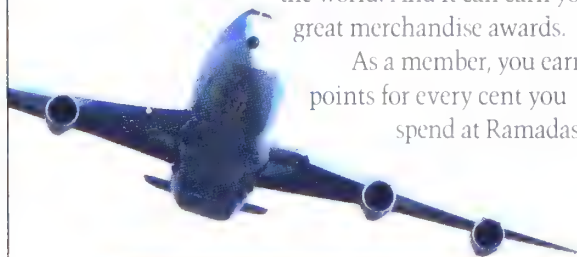
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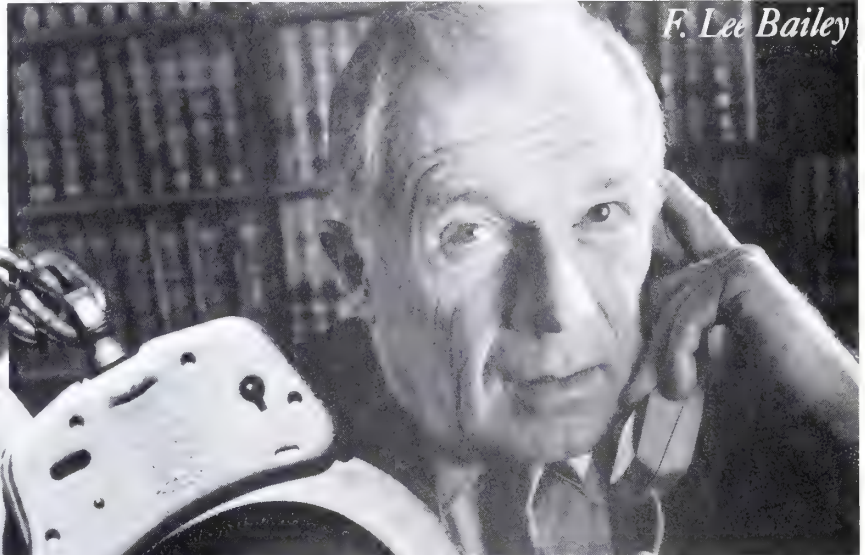
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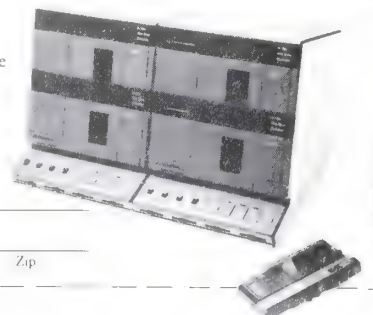
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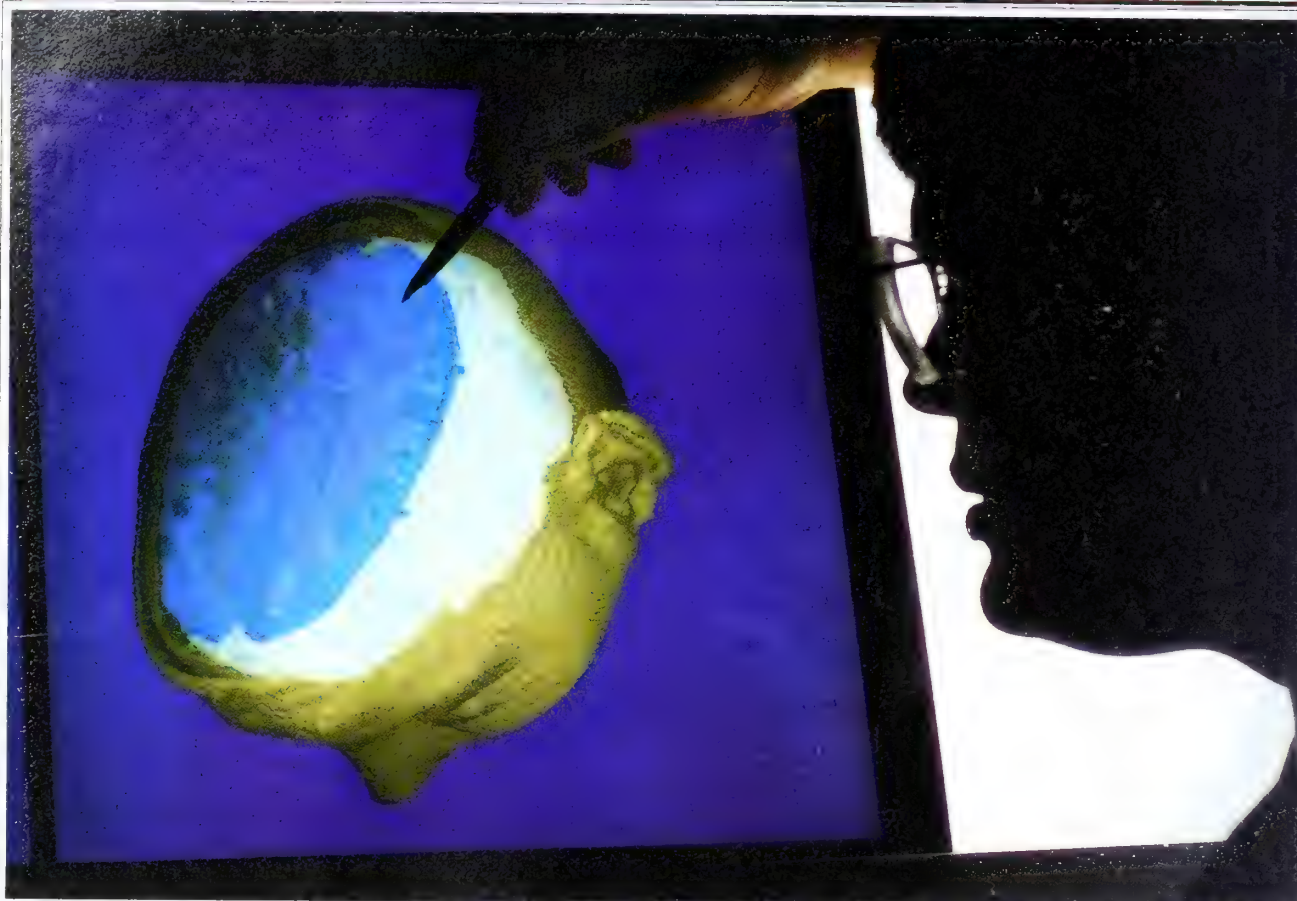


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FINDING NEW USES FOR FILM: A PROTOTYPE 3M COLOR LASER IMAGER CAN CREATE HIGH-RESOLUTION TRANSPARENCIES FROM A CAT SCAN

Cover Story

58 MASTERS OF INNOVATION

Most companies encourage inventiveness, but 3M insists on it. The result: An amazing stream of new products ranging from Post-it notes to heart-lung machines. As nimble as many startups, the giant company nurtures brainstorming by letting employees spend 15% of their time on any product hunch they might have. Sure, they miss a lot, but that's how you produce hits

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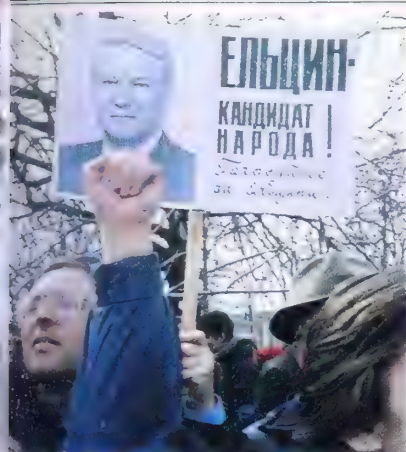
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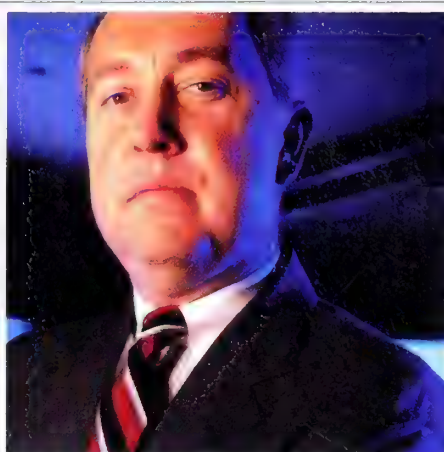
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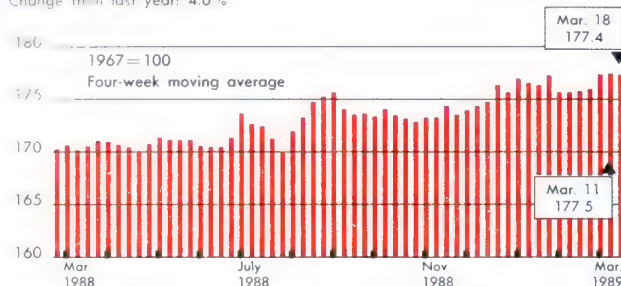
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BusinessWeek Index

PRODUCTION

Change from last week: -0.0%
Change from last year: 4.0%

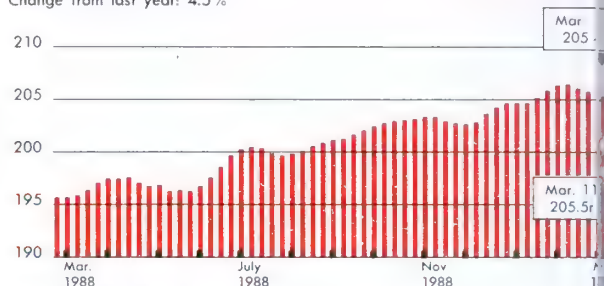


The production index was a shade lower for the week ended Mar. 18. On a seasonally adjusted basis, weekly production of coal, rail-freight traffic, paper, trucks, lumber, and steel increased. However, output of electric power, crude-oil refining, paperboard, and autos all posted declines. Prior to calculation of the four-week moving average, the index dropped sharply, to 176.5 from its level of 177.8 posted the week before.

BW production index copyright 1989 by McGraw-Hill Inc.

LEADING

Change from last week: -0.0%
Change from last year: 4.5%



The leading index edged lower for the week ended Mar. 18. In the last period, stock prices and the growth rates for M2, material prices, and real estate loans were higher, while the number of business failures was down sharply. On the negative side, long-term bond yields continued to rise. Before calculation of the four-week moving average, the index increased to 205.4, from 205.1 in the previous week.

Leading index copyright 1989 by Center for International Business Cycle Research

PRODUCTION INDICATORS

	Latest week	Week ago	% Change year ago
STEEL (3/25) thous. of net tons	2,097	2,057 #	5.1
AUTOS (3/25) units	127,636	152,572r #	-14.9
TRUCKS (3/25) units	68,933	95,450r #	-21.1
ELECTRIC POWER (3/25) millions of kilowatt-hours	51,637	51,187 #	4.7
CRUDE-OIL REFINING (3/25) thous. of bbl./day	12,732	12,548r #	-3.3
COAL (3/18) thous. of net tons	19,934 #	18,634	7.4
PAPERBOARD (3/18) thous. of tons	717.1 #	731.1	-4.3
PAPER (3/18) thous. of tons	775.0 #	760.0r	3.6
LUMBER (3/18) millions of ft.	481.5 #	481.3	-4.1
RAIL FREIGHT (3/18) billions of ton-miles	20.0 #	18.9	5.3

Sources: American Iron & Steel Inst., Ward's Automotive Reports, Edison Electric Inst., American Petroleum Inst., Energy Dept., American Paper Inst., WWPA¹, SFPA², Association of American Railroads.

FOREIGN EXCHANGE

	Latest week	Week ago	Year ago
JAPANESE YEN (3/29)	133	131	125
GERMAN MARK (3/29)	1.89	1.87	1.67
BRITISH POUND (3/29)	1.69	1.72	1.86
FRENCH FRANC (3/29)	6.39	6.33	5.66
CANADIAN DOLLAR (3/29)	1.19	1.19	1.24
SWISS FRANC (3/29)	1.65	1.62	1.38
MEXICAN PESO (3/29) ³	2,392	2,381	2,300

Sources: Major New York banks. Currencies expressed in units per U. S. dollar, except for British pound expressed in dollars.

PRICES

	Latest week	Week ago	% Change year ago
GOLD (3/29) \$/troy oz.	382.950	393.350	-15.6
STEEL SCRAP (3/29) # 1 heavy, \$/ton	118.00	115.50	0.8
FOODSTUFFS (3/27) index, 1967=100	231.5	231.7	6.6
COPPER (3/25) ¢/lb.	145.1	148.1	28.3
ALUMINUM (3/25) ¢/lb.	90.0	94.0	-19.6
WHEAT (7/25) # 2 hard, \$/bu.	4.53	4.59	44.3
COTTON (3/25) strict low middling 1-1/16 in., ¢/lb.	58.57	57.49	-3.1

Sources: London Wed. final setting, Chicago mkt., Commodity Research Bureau, Metals Week, Kansas City mkt., Memphis mkt.

Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1 = Western Wood Products Assn. 2 = Southern Forest Products Assn. 3 = Free market value NA = Not available r = revised NM = Not meaningful

LEADING INDICATORS

	Latest week	Week ago	% Change year ago
STOCK PRICES (3/24) S&P 500	290.18	295.85	9.7
CORPORATE BOND YIELD, Aaa (3/24)	9.85%	9.79%	4.4
INDUSTRIAL MATERIALS PRICES (3/24)	104.3	104.3	5.0
BUSINESS FAILURES (3/17)	268	280	-3.9
REAL ESTATE LOANS (3/15) billions	\$313.9	\$313.1	2.5
MONEY SUPPLY, M2 (3/13) billions	\$3,089.0	\$3,082.4r	0.2
INITIAL CLAIMS, UNEMPLOYMENT (3/11) thous.	336	319	3.1

Sources: Standard & Poor's, Moody's, Journal of Commerce (index: 1980=100), Dept. of Commerce (failures of large companies), Federal Reserve Board, Labor Dept. CIBCIR seasonally adjusts data on business failures and real estate loans.

MONTHLY ECONOMIC INDICATORS

	Latest month	Month ago	% Change year ago
PERSONAL INCOME (Feb.) billions	\$4,315.3	\$4,282.0	3.0
12 LEADING INDICATORS COMPOSITE (Feb.) index	145.2	145.7	3.0
ORDERS FOR DURABLE GOODS: MFG. (Feb.) billions	\$123.7	\$128.1	3.0
REAL GROSS WEEKLY PAY (Feb.)	\$166.75	\$168.21	0.9

Sources: Commerce Dept., BLS

MONETARY INDICATORS

	Latest week	Week ago	% Change year ago
MONEY SUPPLY, M1 (3/13)	\$784.0	\$791.5	1.0
BANKS' BUSINESS LOANS (3/15)	311.8	311.2r	3.0
FREE RESERVES (3/15)	383r	402r	4.0
NONFINANCIAL COMMERCIAL PAPER (3/15)	113.1	110.8	2.0

Sources: Federal Reserve Board (in billions, except for free reserves, which are expressed in millions).

MONEY MARKET RATES

	Latest week	Week ago	% Change year ago
FEDERAL FUNDS (3/28)	9.88%	9.80%	6.0
PRIME (3/29)	11.50	11.50	8.0
COMMERCIAL PAPER 3-MONTH (3/29)	10.08	10.10	6.0
CERTIFICATES OF DEPOSIT 3-MONTH (3/29)	10.20	10.25	6.0
EURODOLLAR 3-MONTH (3/22)	10.30	10.10	6.0

Sources: Federal Reserve Board, First Boston

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OLD-GROWTH LOGGING JUST POSTPONES THE INEVITABLE

As a conservation-minded Northwest-
erner, I appreciated the attempt at
fairness in "Sawmills are starting to
drop like trees" (Top of the News, Feb.
6). You made the point that environmen-
talist lawsuits exacerbated an exist-
ing condition, rather than caused it.

For decades the Forest Service and
Bureau of Land Management have been
offering timber for sale at levels far
higher than could be sustained. Our old-
growth timber in the Northwest has
been "mined," not "harvested." Current
biological research indicates that the fu-
ture health of our forests for long-term
sustainable yield depends on the contin-
ued existence of large old-growth
stands. If we are to have any chance of
retaining our forests as a renewable re-
source, we need to keep our options
open now and limit the cut.

There are millions of acres of second-
growth forest that can be logged, and
they will be, when we run out of old-
growth. Whether the government allows
most of the old growth to be logged
immediately or not, timber companies
still face the need to retool the mills and
update old equipment. Why must we put
off that day of reckoning at the price of
destroying an irreplaceable ecosystem?

Carolee Colter
Community Consulting Group
Seattle

DRIVERS ARE LICENSED, SO WHY NOT GUN OWNERS?

I endorse the title of your editorial,
"There's no 'right' to bear semiauto-
matics" (Editorials, Mar. 13), but not
your prescription on how to "stop another
Purdy from plunking down his money
and taking more innocent lives." You
advocate banning private possession not
only of the kind of semiautomatic rifle
Patrick Purdy used in the Stockton
schoolyard massacre but semiautomatic
firearms in general. Aside from the im-
pact of such a ban on the legitimate
interests of qualified, law-abiding gun
owners, banning these weapons would
leave other guns easily accessible to the

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Pizzarelli at 212 512-6246.

likes of Purdy and other individuals
clearly lacking the crucial qualifications
for responsible gun possession.

The nation needs a permit system for
possession of all kinds of usable fire-
arms and some means of holding gun
owners strictly responsible for the safe-
keeping, legal use, and legal transfer of
every gun they own. Upgraded permits
should be required for semiautomatic
firearms, just as a special driver's li-
cense is required for operating a bus, a
tractor, a truck, or a motorcycle. Dis-
playing an appropriate gun-owner's li-
cense should be required for purchases
of ammunition.

These proposals are not antigun.
Rather, they may well be essential to
the survival of private gun ownership in
America.

David J. Steinberg, Executive Director
National Council for a Responsible
Firearms Policy Inc.
Alexandria, Va.

Your editorial focused on the rifle
and the fact that it was a "semiauto-
matic" as the cause of the crime. Such
an approach obscures the true criminals:
Patrick Purdy and the California criminal
justice system. Mr. Purdy purchased
the weapon involved after satisfying the
local waiting period. Since he had been
allowed to plea-bargain several offenses
from felonies to misdemeanors, he was
not on record as a convicted felon. What
has failed is the criminal justice system.
BUSINESS WEEK appears to be adding its
voice to the throng of those who refuse
to understand that life provides many

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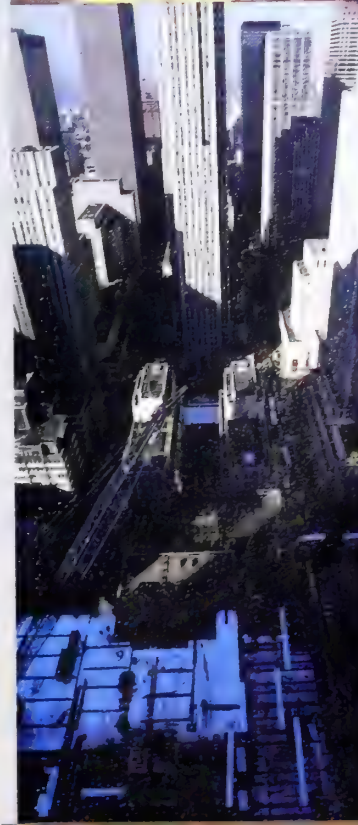
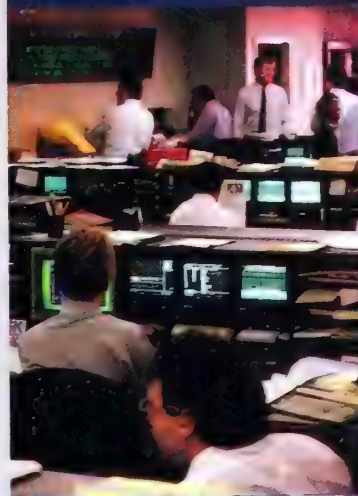


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Readers Report

opportunities for the misuse of dangerous substances and objects. Why not prohibit cars, since drunk drivers kill and maim far more people each year in firearms? The list of examples is endless. Either we as a nation exert the will to imprison criminals for substantial time spans or we will eventually have to ban all activities that distinguish Americans as a free people.

Rather than suggesting yet another law, perhaps your editorial should have demanded the enforcement of existing laws. People like Purdy will always exist. The way to deal with them is with a national criminal justice system, not taking away from honest citizens a right so sacred the Founding Fathers secured it just after freedom of speech.

Theodore I. Kornfeld, Vice-President
Kidder, Peabody & Co.
New York

To suggest that you could somehow ban any type of weapon when we cannot keep shiploads of cocaine off our streets is ludicrous. But the proposal at seems most inappropriate from a business magazine is the economics of it. It would cost billions of dollars to implement your plan. Rather than squander these funds, we should put them to use in our police forces fighting crime. It makes no business sense to waste this money policing law-abiding citizens who, after all, are not the problem.

F. C. Greer
Fort Valley, Ga.

THE IVORY TOWER IS NO HELTER FROM FICA TAXES

I think Richard Brubaker of Dayton has been misled about who is exempt from Social Security withholding ("Should the Social Security system be retired?", Readers Report, Feb. 13). Both my husband and I have worked for the University of Utah and the University of Kansas, he as faculty, me as staff, and at both state universities, FICA was automatically withheld from our checks, just as it has been at the other publicly held and privately held, for-profit and not-for-profit places where we have worked over the past 25 years.

Peg Hogben
Tulsa

AT&T DENIES TRYING TO WIN POLITICAL SUPPORT IN ITALY

We read with interest and some surprise the telecommunications report, "Dealmakers are burning up the phone lines" (Special Report, Mar. 13), that focused in part on American Telephone & Telegraph Co.'s efforts to de-

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Readers Report

lop an alliance with Italtel, Italy's state-owned equipment manufacturer. Our surprise came from the reference our having offered to make investments designed to win political support in Italy. Not one dollar of investment was proposed as a political centive. The agreement that was reached was clearly based on its commercial and technological merits. riod.

While BUSINESS WEEK may have been ld otherwise, the reference is not facial. The unnamed source was not in a sition to speak for the company.

Robert E. Allen
Chairman

American Telephone & Telegraph Co.
New York

AMERICAN TOBACCO IS DOING MORE IAN JUST WHEEZING ALONG

Your article on tobacco manufacturers, "The cigarette makers: Just neezing along" (Marketing, Jan. 23), indicated that our American Tobacco Co. bsidiary experienced a decline in its are of the U.S. cigarette market. Actually, American Tobacco outperformed e industry as a whole in 1988, accord-

CORRECTION

"Is your company too big?" (Cover Story, Mar. 27) drew upon data that did not contain 1988 results to compare performance of companies in four industries. Here are the updated figures:

	1988 Revenues Millions	Three-year averages Return on equity	Sales growth*
International Paper	\$9,500	11.8%	28.7%
P.H. Glatfelter	569	20.7	27.1
Wal-Mart Stores	20,600	28.5	34.7
Jamesway	783	9.6	14.4
LTV	7,300	NM	-3.7
Birmingham Steel	344	18.3	32.4
Merrill Lynch	10,500	14.0	14.0
A.G. Edwards	475	14.7	5.5

*Compounded NM: Not meaningful NA: Not available
DATA: S&P COMPUSTAT PC PLUS

ing to Management Science Associates (MSA), an independent organization which compiles statistical information based on historic industry data. MSA's figures indicate that American Tobacco's market share rose to 6.96% in 1988 from 6.92% in the prior year.

Contributing to this gain was the continuing success of Malibu and Pall Mall

Red Filters (rolled-out nationally in 1987) and American Lights (introduced nationally in 1987) as well as an increase in market share by Carlton. These are the industry's leading ultra-low-tar brands.

Robert J. Rukeyser
Vice-President
American Brands Inc.
Old Greenwich, Conn.

MORE COMMENT ON GIANCARLO PARRETTI

In your recent article on Cannon Group Inc.'s new financiers ("Puzzle in movieland: The case of the mystery moguls," Entertainment, Mar. 13), your writers made reference to my having been introduced to Giancarlo Parretti. I have never met nor spoken with Mr. Parretti.

Michael S. Ovitz
Creative Artists Agency Inc.
Los Angeles

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IRRECONCILABLE DIFFERENCES: ROSS PEROT VERSUS GENERAL MOTORS

By Doron P. Levin

Little Brown & Co. • 357pp • \$18.95

AN INSIDE LOOK AT A BITTER CORPORATE DIVORCE

Uh, oh. When General Motors Corp. Chairman Roger B. Smith reads this book, he's likely to throw one of his legendary tantrums. As if he didn't have enough problems, what with GM's U.S. car operation falling to an unheard-of 34% market share despite tens of billions of new dollars invested. Now comes *New York Times* and former *Wall Street Journal* reporter Doron P. Levin to retell in excruciating detail the dismal tale of Smith's ill-conceived 1984 purchase of Electronic Data Systems Corp. and his ensuing five-year spitting contest with its founder, H. Ross Perot. The title, *Irreconcilable Differences*, fits: For you GMers out there, it will be like reading an account of your failed marriage as written by your ex's divorce lawyer.

It isn't light reading. But it is fascinat-

ing, spiced with new details of the Smith-Perot fight and offering a rare glimpse into high-powered corporate politics. As Levin tells it, Smith cut a bad deal, paying top dollar for EDS and promising Perot freedom to run it, and then weasled out of the parts he didn't like. Perot comes off as a victimized good guy, Smith as his brilliant but temperamental persecutor. Still, it's hard to feel sorry for Perot, who sold EDS for \$2.55 billion, then received \$738 million to get lost and shut up—but didn't.

At first the pettiness, vindictiveness, and Machiavellian moves by Smith and Perot seem comical. But as the war escalates, you get a gloomy feeling about the venality and ruthlessness of corporate life, the everyday use and abuse of power and money. (For lighter companion reading, try former GM speechwriter

Albert Lee's irreverent look at Smith in *Call Me Roger*, just out in paperback.)

The big question about *Irreconcilable Differences* is, how fair is it? No doubt Levin looked at both sides. But Levin doesn't like controversy, especially when it concerns Perot, and it's evident that Levin didn't get much from Smith's rebuttal of what must have been an earful from Perot and his people. Indeed, many times Levin writes as if he were Perot's advocate. He sympathetically explains the rich stock-incentive plan Perot insisted on for his employees, which Smith bridled at. Yet he derides GM's bonus plan as a gravy train for lackluster executives. His GM managers are petty bureaucrats protecting their turf by blocking EDS teams sent in to run computer telephone systems. But he ignores well-founded gripes that inexperienced EDSers came on like storm troopers and often bungled the job.

The imbalance is exacerbated because on the advice of his lawyers, Levin omitted attributions that might make him or his sources party to litigation between Perot and GM. (EDS is suing Perot for starting a computer company despite a three-year noncompete pact.) The reader never knows where Levin



you'd think that you had nothing better to do with

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t his juicy tidbits about
emos, meetings, and
versations. So despite
arning detail about how
ith welched on his
omises, there's a credi-
ity problem.

Levin concludes that
rot went public with his
t criticism of Smith's
management style only to
ake Smith live up to the
EDS deal. But what if
rot, the shrewd son of
East Texas cotton trad-
was all along angling
be bought out by mak-
g himself a pest? What
his quixotic public cam-
ign to reform giant GM
is just a way of banging
cup on GM's gold-plated jail bars?

Perot had to know GM would be hard-
to turn around than a Cadillac in a
nd alley—with no power steering. And
a seasoned executive he offers some
ther hollow criticisms. GM's board is
st a rubber stamp for the CEO? That's
re at lots of big companies. Smith is a
nperamental bully? You'd scream and
m red, too, if you had to run GM's
odgy bureaucracy. GM paid way too
ch for Hughes Aircraft and EDS?



WHY ARE THESE MEN SMILING? LEVIN'S ACCOUNT OF THE PEROT-SMITH FEUD LEAVES A GLOOMY IMPRESSION OF VENALITY AND RUTHLESSNESS IN BUSINESS

(Yes, Perot even complains about that.) They'd be cheap at twice the price, considering that GM is long on money and short on ideas for its future.

Levin seems convinced that Perot sold back his GM stock and left GM's board only when relations with Smith soured beyond repair. He apparently accepts the hard-to-swallow claim of Perot's lawyer that Perot didn't know of the buyout plan until it was presented to him as a done deal. The only hint that Perot had

greenmail in mind comes from Elmer W. Johnson, who appears to be Levin's main high-level GM source. As GM's top lawyer, Johnson negotiated Perot's 1986 exit, and he says the buyout idea came early on from Perot's side. But Johnson comes across as only a halfhearted Smith advocate. No wonder: While once seen as a potential successor to Smith, Johnson left GM in 1988 after voicing many of the same criticisms Perot had raised, especially about GM's failure to tie salary to performance. The lack of any other GM response

to Perot's version reinforces the impression that Smith cashed Perot out as a costly but expedient way to squelch dissent.

Behind GM's wall of silence, you can bet there's still one helluva story to be told about what went on inside GM over EDS. But until it is, Levin's half a tale is better than none.

BY JAMES R. NORMAN

Former Senior Writer Jim Norman covered GM in BW's Detroit bureau.

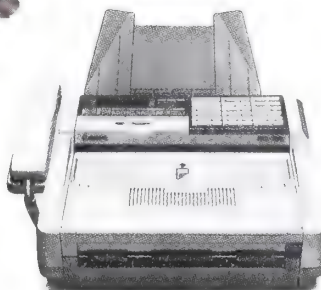


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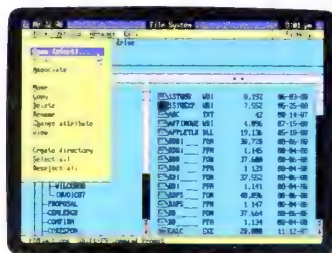
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HOW BAD WILL THE NEXT DOWNTURN BE? FLIP A COIN

BY GARY S. BECKER



They talk a good game, but economists hardly know enough about business cycles to figure out where they come from, let alone where they're going. So, be wary of those predictions of a gentle contraction

Some people believe that the expansion and contraction of business cycles in the U.S. are becoming tamer because of the length of the current expansion, now in its 76th month. Aside from one during the Vietnam War, this boom is the longest since the end of World War II. However, just as one swallow does not make a spring, one unusual boom doesn't say much about the future course of business cycles, and I doubt that the business cycle is becoming any gentler.

The sad fact is that economists, including the experts on business cycles, do not know why booms invariably come to an end. And they know little more about why recessions—be they severe or mild—draw to a close. This is true despite an enormous effort devoted to theoretical and statistical studies of cycles during the past hundred years.

Economists are not even sure whether business cycles are self-generating, continuing on their own steam because of the internal logic of markets and economies. It could well be that each cycle represents a unique response to external shocks, such as the sharp rise in oil prices during the early 1970s, or bad monetary and fiscal policies.

UNRULY BUNCH. The truth is that the term "business cycle" is itself a misnomer, for economies are subject to fluctuations, not repetitive cycles of similar lengths and amplitudes. Expansions and contractions vary greatly in length. For example, although the nine post-World War II expansions averaged only 48 months, two besides the current one exceeded 55 months, and two were shorter than 25 months.

The current boom followed the worst depression of the postwar period—from July, 1981, to November, 1982. There was a lot of slack in the economy when business began to improve—unemployment exceeded 10.5%, and industry had much unutilized capacity. It should be no surprise that the subsequent boom proved long and buoyant.

Many bankers and economists believe that the length of the boom is also the result of wise monetary policy by the Federal Reserve. Some even claim that it could continue more or less indefinitely if the Fed does not overreach in the fight against growing inflation. And there's no reason to doubt the Fed would pursue such a course. The problem is, it just doesn't know how.

Others explain this long expansion and their hopes for mild cycles in the future by various programs of the Reagan Administration. In particular, they cite greatly reduced personal tax rates and other supply-side policies, deregulation, a lower value of the dollar, and the

budget deficits. Many of these programs have improved the economy's performance, but no one has shown that they have much relevance for the severity of business cycles.

In the past, unwarranted optimism or pessimism often followed one unusual episode. The Depression convinced many prominent economists in the 1930s that capitalist economies could no longer generate full employment without massive assistance from government spending. These economies were alleged to suffer from "secular stagnation," a term coined by Alvin Hansen, then a well-known professor at Harvard. The boom after World War II and throughout most of the 1950s and '60s killed all talk of continued stagnation.

Decades after the Depression, in the latter half of the 1950s and first half of the 1960s, when prices in the U.S. stayed rather stable, some economists predicted an end to serious peacetime inflation. Yet the most severe bout of peacetime inflation in U.S. history occurred shortly afterwards, in the 1970s.

SCARE BEARS. A more recent example of such extrapolation from events was the widely shared—but erroneous—belief at the time that the stock market crash in October, 1987, would be followed by a depression propelled by a sharp drop in investments and consumer spending. A false analogy was drawn from the Depression, which followed not long on the heels of the 1929 crash. This pessimism about the economy has been forgotten by many as the present boom continues unabated after the crash.

A number of economists, myself included, went against popular opinion and forecast that the crash would not have a major effect on the U.S. economy. We were right not because we had profound insights into the causes of business cycles and the operation of stock markets—I certainly don't—but because we believed that the experience of 1929 held few lessons for 1987, since we doubted that the 1929 crash caused the subsequent depression. Moreover, the economy looked strong in October, 1987, and even the 25% decline in stock values only slightly reduced the total wealth of the vast majority of workers and consumers.

Given the business cycle experience of the past half-century, there isn't any reason to believe that the next contraction will be especially mild. The lesson is that the U.S. economy will continue to have serious recessions—and the length of the expansion that precedes them tells us little about how severe they will be. But I repeat my warning that we economists cannot predict business cycles very well.

GARY S. BECKER IS UNIVERSITY PROFESSOR OF ECONOMICS AND SOCIOLOGY AT THE UNIVERSITY OF CHICAGO



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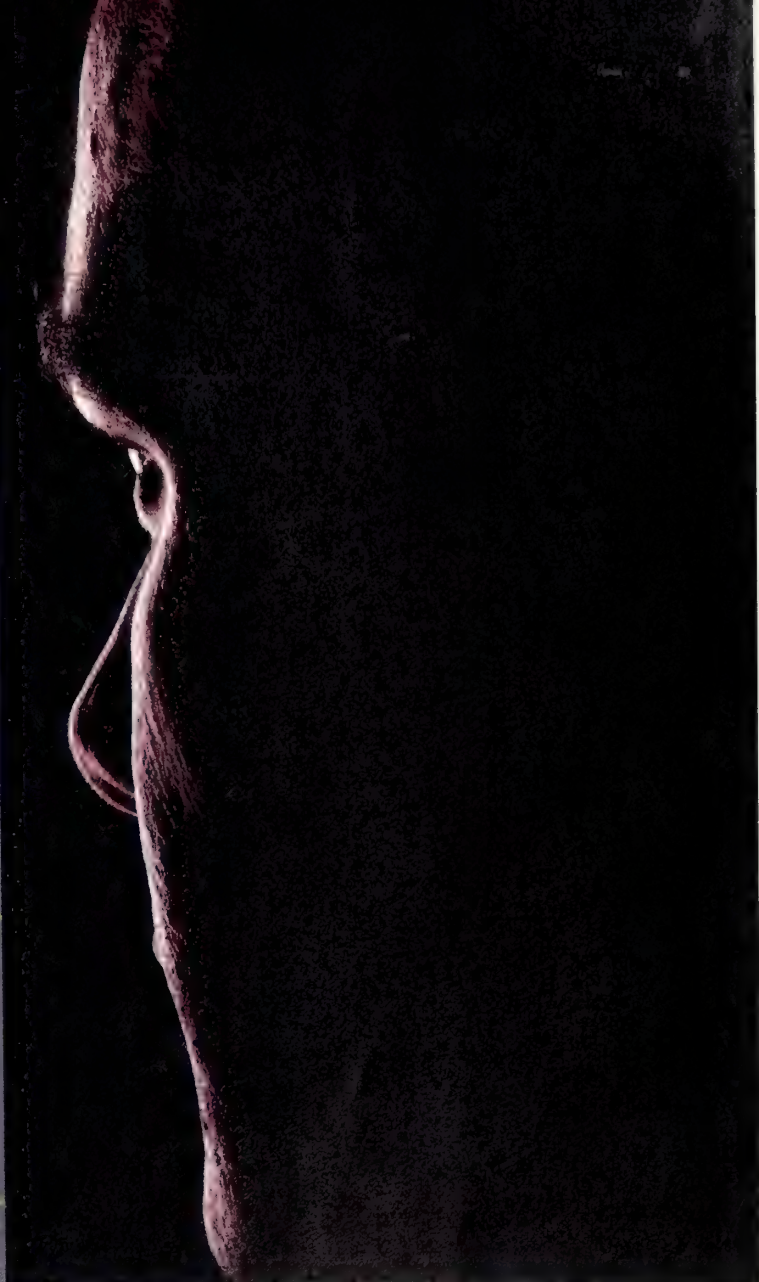
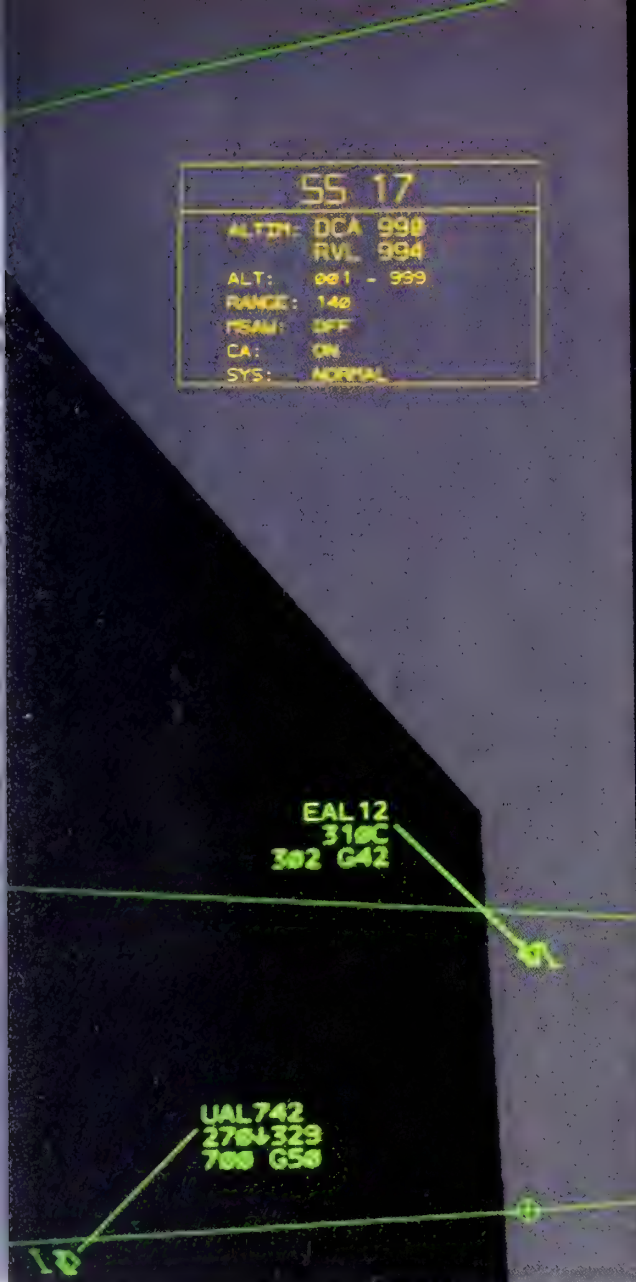
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Where quality starts with fundamentals

BY MICHAEL J. MANDEL

WITH A REPUBLICAN IN OFFICE, A RECESSION MAY BE LURKING . . .

Presidential election results may be a good way to predict economic downturns. That is the conclusion reached by economists Alberto Alesina and Jeffrey Sachs of Harvard University after examining the postwar economic record. Since 1948 the Republican Party has won six Presidential elections, and five of them were soon followed by recessions. The only Democratic recession came in 1980, at the end of Carter's term.

"In the first half of a Republican Administration, you get the hard medicine to hold down inflation," notes Alesina. By contrast, the Democrats, it seems, are more concerned with boosting output. These differences are not immediately apparent after the election, since it takes six to nine months for a change in policy to take effect. But then it becomes very easy to tell who won the race: just look at real economic growth in the victor's second year in office. On average, it's 6.2% for the Democrats and

Republicans and Democrats starts looking more alike in the second half of their terms—in both cases, about 4% real growth in gross national product. By their fourth year the Republicans produced a slightly higher growth rate.

This seems to be an example of good planning by the Republicans. They take a recession early in their Administrations and then enjoy moderate growth at the end. While this helps explain their success in winning elections, it does have a cost: On average, the economy grows much more slowly under the Republicans. The Democrats have won fewer elections, but they have produced more economic growth. Alesina concludes: "Democrats and Republicans really are different."

. . . AND IF IT COMES, THE POOR WILL REALLY TAKE A HIT

If, true to form, a recession does arrive in the second year of the Bush Presidency, who's going to be hurt the most? The perhaps unsurprising answer: the poor. But the extent to which low-income households suffer in a recession may come as a surprise. According to research by Rebecca Blank of Princeton University, during an economic downturn the income of the poor drops almost twice as fast as the income of high-income households. "Households headed by black men and by people under the age of 24 are especially vulnerable," says Blank. "If GNP falls by 1%, their income will on average fall by more than 1%." The reason: Falling wages and increased unemployment hit the poor harder than high-wage earners.

Blank's findings are based on survey data from the University of Michigan, but evidence from the Census Bureau bears out her conclusions. From 1979, a peak year of strong economic growth, to the recession in 1982, average real income of the poorest fifth of all U.S. families fell by 17%. By contrast, the average real income of the wealthiest fifth of families fell only by 6%.

Interestingly, the poor generally increase their share of personal income during expansions. But the current business cycle has been a troubling exception. Census data show that from 1982, the beginning of the expansion, to 1987, the average real income going to the poorest families increased by 8%. However, the average real income of the wealthiest families rose even more, by almost 16%. "This time the poor haven't caught up," reports Blank. And that means, she concludes, that the gap be-

tween low-income and high-income households will widen further when the next downturn comes.

SURE, HIGHER RATES WILL SLOW THE ECONOMY—BUT SLOWLY

Waiting for high interest rates to slow down the economy? Don't hold your breath. "Higher rates used to have a direct effect on the domestic economy," says William Dudley, senior economist at Goldman, Sachs & Co. "Now they have to work indirectly through the exchange rate and foreign trade, where the lags are much longer."

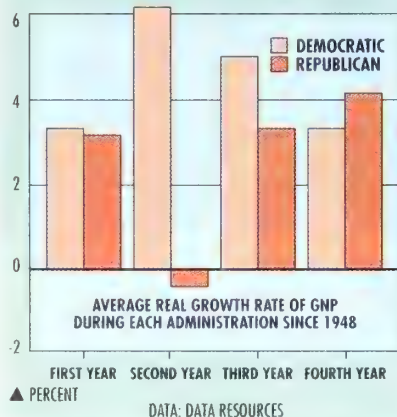
For one thing, Dudley notes that changes in the housing market have dulled the impact of rising rates, so that housing activity has hardly slowed in the last year. While higher rates do increase the cost of adjustable-rate mortgages and home equity loans, Dudley estimates that a 2% rise in interest rates would only increase aftertax interest expense to households by \$7 billion—just 0.2% of disposable personal income. Dudley also argues that business fixed investment has become less sensitive to interest rate changes, citing access to junk bond markets, which insulate corporations from higher short-term rates.

That leaves trade as the major sector affected by interest rates. "When rates go up, the dollar appreciates, trade deteriorates, and the economy slows," says Dudley. The problem: It's a slow process that may require even higher rates to exert an effective brake on economic activity.

THE RUST BELT SHOWS A LOT MORE SHINE

The 1980s were the bicoastal decade. Both coasts thrived during the expansion. But the nation's heartland is getting a lot sturdier, suggests a recent report by Steven R. Malin, regional economics director for the Conference Board. He notes that in the Midwest, rising export orders in manufacturing have spurred growth in business and financial services and strengthened nonresidential construction. "There's been a change in the mix of occupations compared with the early 1980s," says Malin. "The result is that the region will fare better during the next contraction." But he warns that unlike some parts of the country, the Midwest needs healthy exports and strong manufacturing to sustain growth in service employment.

THE GOP PRESIDENTS' SOPHOMORE SLUMP



only -0.4% for the Republicans (chart).

Both parties have been consistent in their second year. No Democrat has produced over less than 5.3% real growth, while no Republican has produced more than 2.8%. With the exception of Reagan's second term, the economy has shrunk in the second year of every postwar Republican Administration.

If George Bush follows the same pattern, says Alesina, the historical evidence predicts "a mild recession at the end of 1989 or the beginning of 1990." But then the economy should begin to turn up, because the economic record of

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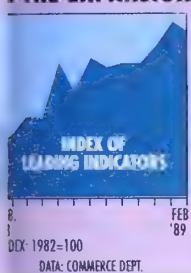
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THE SLOWDOWN IN CONSUMER SPENDING MAY BE ONLY A BREATH

The consumer is still the most important player in this economic expansion. Consumers account for about two-thirds of gross national product, and they behave this spring will go a long way toward determining the economy's strength and inflation's potential. That, in turn, will decide how much further the Federal Reserve Board will tighten monetary policy—where interest rates will head.

THE FED'S STILL VERVE IN THE EXPANSION



Right now the economy isn't showing much loss of momentum. The government's final look at real GNP for the fourth quarter produced an upward revision from 2% to 2.4%. Adding back the 1.1 percentage points taken away by the drought puts the growth of the nonfarm economy at a robust 3.5%.

First-quarter growth, even after accounting for the expected drought jump in farm output, is shaping up to be strong as well, but quite different in composition. The ease of consumer spending, strong in the fourth quarter, is much weaker in 1989's first quarter. Capital spending, which dropped at yearend, appears to have rebounded. And the trade deficit, after a huge deterioration, has probably improved somewhat. The Commerce Dept.'s index of 12 leading indicators shows little evidence that any lasting slowdown is on the way. The index did dip 0.3% in February, but its trend remains firmly up (chart). The leading index has risen 1% over the past year, up from 2.4% during the previous year.

THE FAST FED MOVES ARE MAKING A DIFFERENCE

The best clues to the economy's strength will come from consumer spending—and that's where the Fed most wants to see a slowdown. True, spending cooled off in the first quarter. But will that slowdown last? The stubborn strength of the consumer sector has confounded forecasters throughout this expansion. This latest quarterly lull may well turn out to be as ephemeral as others in the recent past.

The driving forces behind consumer buying are as strong as ever. Unrelenting job growth is generating income at an increasing pace. And consumer confidence remains historically high. So far, all this has more than offset the Fed's yearlong attempt to dampen spending with higher interest rates.

Since last March the Fed has pushed up interest rates

using the federal funds rate—the charge on interbank borrowing—as its key policy tool. That rate has soared from 6½% to just under 10% at the end of March, 1989.

Other short-term rates have followed. The yield on three-month Treasury bills, for example, has risen from a bit more than 5½% to a shade below 9½%. Long-term interest rates are also up, but not by as much. As a result, the costs of both fixed- and variable-rate consumer loans are substantially higher than a year ago.

In fact, a few early signs of the impact of past Fed tightening are starting to show. Housing demand is weakening. Sales of new single-family homes tumbled 9.4% in February, to a 626,000 annual rate. That puts sales 4.6% below their year-ago level. Purchases of existing homes also dropped, falling 3.1%, to a yearly pace of 3.44 million. That followed on the heels of a large 9.4% decline in January.

Another possible sign: the persistence of weak car sales in the middle of March, when Detroit's most liberal incentive program in months was in full swing. Sales of domestically made autos rose to only a 6.8 million annual rate from a poor 6.2 million showing early in the month. Sales in both January and February were at 7 million.

SERVICES GRABBED MORE DOLLARS

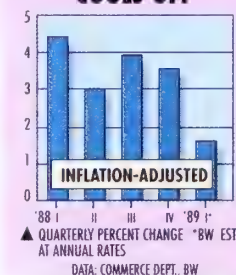
When the Fed held its policy meeting on Mar. 28, it undoubtedly took into account these recent signs of slowing in the consumer sector. That may help relieve some of the central bankers' worries about inflation for now, but it's still not clear if that slowdown will last.

In February consumers increased their purchases by a healthy 0.5%, to an annual rate of \$3,375.7 billion, following a 0.4% rise in January. Much of the February gain came from increased energy use, which returned to more normal winter levels after January's warm-weather respite. Indeed, after adjustment for prices, real spending rose 0.4% in February, reversing the 0.3% loss posted in January.

February's performance indicates that first-quarter growth in real consumer spending will be the weakest in more than a year. Even if inflation-adjusted buying in March matches the February increase, purchases for the entire quarter will be up by only 1.6% at an annual rate, far below the 3.5% pace in the fourth quarter (chart).

Real spending on goods was essentially flat in Febru-

CONSUMER SPENDING COOLS OFF



Business Outlook

ary, as it was in January. Inflation-adjusted purchases of durable goods fell 0.2% in February, following a 3.8% plunge the month before. Sluggish car sales were the biggest cause.

Real purchases of nondurable goods also fell in February, by 0.1%, but they had jumped 1% in January. Sluggish sales of food and clothing led the February weakness, but the cold weather boosted fuel use by 11.5%.

Services, however, rose a strong 0.9% in February, even after adjusting for prices. One-third of the gain came from a 7.2% jump in electricity use, but spending on education also rose.

Judging by the continued weakness in car sales in March, spending in that month is not off to a good start. And with auto inventories already high, a pickup in car buying in late March will be critical if Detroit is to avoid production cutbacks. Detroit made cars at annual rates of 7.5 million in January and 7.2 million in February.

But excluding autos, sales probably did better in March, if only because Easter fell early this year. That will boost the March numbers on spending, but as usual it will steal some strength from the April sales data.

The slowdown in spending did boost the savings rate in the first quarter, but that usually happens when car sales drop. Still, the rate has been trending higher. In the three months ended in February, personal savings as a percent of aftertax income stood at 5.2%. That's up from 4.2% for all of 1988 and from 3.2% in 1987.

INTEREST INCOME ZOOMS HIGHER

The weakness in consumer spending is likely to be short-lived. For one thing, consumers are still in good spirits. The Conference Board's index of consumer confidence remains very high. Although it fell in March, to 117.7 from 120.7 in February, it was still well above the 115.2 average of the previous year.

For another, consumer purchases of services and nondurable goods—some four-fifths of all spending—are not

so sensitive to interest rates. And income growth the past few months has been too strong for consumers to stop spending for long. Higher interest rates dampen sales of some durable goods, but strong income gains will keep fueling spending elsewhere.

In February personal income advanced by 1%, to an annual rate of \$4,315.3 billion. January's gain was an even sharper 1.7%. An increase in farm subsidies boosted February earnings, but even excluding those payments, income growth was still robust, rising 0.7%.

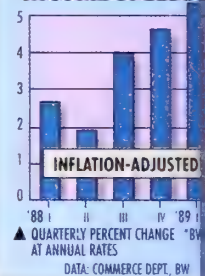
Wages and salaries—the bulk of personal income—increased a healthy 0.6% in February, following a 1.1% jump in January. Services and the distributive industries, such as wholesale trade and transportation, accounted for the bulk of the February gain. Factory earnings also rose, but not by as much.

So far this year income growth has been impressive. In the first quarter, real nonfarm income, after adjusting for prices, appears to have grown at a 5.3% annual rate (chart). Income growth has been accelerating three consecutive quarters, and the first-quarter pace shaping up to be the fastest in five quarters.

Rising interest rates are also benefiting many consumers. Interest income, which accounts for a bigger share of personal income than earnings in manufacturing, continues to lead all income growth. Interest earnings surged 1.4% in both January and February and stand 13.4% above a year ago. All other income has grown by a slower, but still impressive, 8.7% over the same 12 months.

These solid supports mean that consumer spending is likely to pick up again in the second quarter. If so, despite further Fed tightening—and higher interest rates—

NONFARM PERSONAL INCOME SPEEDS



THE WEEK AHEAD

NAPM SURVEY

Monday, Apr. 3

The index of business activity compiled by the National Association of Purchasing Management will probably decline to 52.5% for March. In February the index dropped to 53%. The NAPM surveys its members, mostly industrial companies, on current business conditions, including hiring plans and export orders. The index has been sluggish in recent months, but a reading above 50% indicates that the economy is expanding.

CONSTRUCTION SPENDING

Monday, Apr. 3, 10 a.m.

Spending on building projects most likely fell by 1.5% in February after rising

0.4% in January. The February decrease is indicated by the 11.4% drop in housing starts, a decline in construction jobs, and the return to more normal winter weather, which inhibits construction activity.

CAR SALES

Tuesday, Apr. 4, 4:15 p.m.

New domestically made cars probably sold at an annual rate of about 7.2 million during the last 10 selling days of March, despite liberal financing incentives. For all of March, new cars likely sold at an annual rate of 6.7 million. That would be the slowest monthly pace since November, 1987, and may well lead auto makers to cut second-quarter production plans. U.S.-made cars sold at a 7.1-million pace in February.

EMPLOYMENT

Friday, Apr. 7, 8:30 a.m.

Most economists expect that nonfarm payrolls increased by a moderate 22,000 new jobs in March, following a strong 289,000 gain in February. With the labor market still expanding, the March unemployment rate probably remained at the low 5.1% level of February.

INSTALLMENT CREDIT

Friday, Apr. 7

A \$2 billion gain in consumer debt is likely for February, compared with January's \$4.4 billion rise. This small increase is suggested by the February drops in new-car sales and in purchases at department stores.

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THE VOTE HEARD ROUND THE WORLD

THE SOVIET PEOPLE GIVE GORBACHEV'S REFORMS A HUGE BOOST

They were the freest Soviet elections in 72 years—and, not surprisingly, the most portentous.

A slate of Lithuanian nationalists upset two Communist Party bosses. Boris Yeltsin, the outspoken populist whose face appeared every night on America's news, trounced the old-guard Communist in charge of making party bosses' limousines. Across the Soviet Union, candidates were pushing radical solutions—from environmentalists seeking tighter controls to those demanding action on the country's food, housing, and consumer goods shortages. They all scored in races for the new Congress of People's Deputies.

But the biggest winner of all was Mikhail S. Gorbachev, who was handed a people's victory he couldn't have foreseen. In Moscow, Leningrad, and Kiev, voters strongly rejected Communist Party conservatives and backed reformers. In some places where party bosses ran unopposed, angry Russians struck the names off ballots, forcing new elections for those seats. Of 180 million eligible voters, 85% cast ballots.

As the outcome became known, Soviets were still grappling with the meaning of what they had wrought. Lev Timofeyev, publisher of an independent newspaper, sounded an optimistic note: "This shows the rest of the world that the reform process is ongoing, despite the obstacles." Others warned of difficult times ahead. Says Nikolai Shmelev, a reform-minded economist in Moscow: "In our parliament we will have a very influential group of quite independent people. [Soon] no law, no government decision will be [made] without varied discussion. For a government such as ours, it will not be an easy time."

GRASS-ROOTS RALLIES. The vote offers Gorbachev badly needed momentum to keep his twin economic and political programs moving ahead, while continuing to promote his initiatives abroad. His most urgent domestic problem is to overcome resistance to freeing markets,

prices, and jobs. The unprecedented grass-roots rallies and voter turnout show that millions of Soviets want a change, and that freer speech and a freer economy aren't just the dreams of Moscow intellectuals.

Even more far-reaching, the election could give Gorbachev the backing he needs to prune party hacks who ran badly or were scribbled out on ballots. Officially, the full vote tally won't be ready until Apr. 5, but just two days after the election, Soviet Foreign Ministry spokesman Gennady Gerasimov hinted that big losers may have to "reassess" their positions and perhaps give up power on grounds that they are no longer credible party delegates.

These fledgling steps toward democra-

cy are also likely to raise Gorbachev's stock abroad—just days before he meets Britain's Prime Minister Margaret Thatcher and weeks before the Bush Administration completes a crucial review of U.S. policy toward the Soviet Union.

The vote seems likely to exacerbate divisions within the Bush Administration over American policy toward the Soviet Union. For now, those pushing for further liberalization of East-West ties look stronger. A key goal of this bloc is to ease the limits on Soviet imports of Western technology.

As if to foreshadow the benefits to ensue, the new American Trade Committee, a group linking six U.S. companies, planned a Kremlin ceremony on Mar. 30 to sign an agreement to co-



A MASSIVE VICTORY BY YELTSIN (TOP LEFT) AND DISMAY OVER SAKHAROV'S EXCLUSION SHOWN

eral giant joint ventures with the So-
Union (page 38).
et there are still plenty of hardliners,
pecially at the Pentagon, who see a
side to this surprising outbreak of
iet democratization. Their argument:
election turmoil could make the So-
government even more unstable—
perhaps more dangerous. After all,
argue, if senior party bosses are so
erable, Gorbachev could be, too.
hen, too, there's the sobering reality
the Mar. 26 election was hardly an
ecise in Western-style democracy. Of
2,250 seats at stake, 750 had been set
for handpicked candidates of the
munist Party and official groups
as the Academy of Sciences. And
some of the remaining 1,500 seats,
one candidate was nominated.
or Gorbachev, the reformist victories
n't without risk. No one knows how
d militant nationalists, who made im-
tant gains in the Baltic states and the
aine, will push for more autonomy
n Moscow. An even greater risk is
possibility that the election may have
ed voters' hopes for better living
adards to a level Gorbachev can't
e to meet. Indeed, in the short term,
sening conditions seem inevitable,
e a key element of *perestroika* in-
ves higher prices for food, housing,
clothing.
he final makeup of the legislature

remains an open question. The Congress
of People's Deputies will only meet a
few times a year, starting in late April,
when it will elect from its ranks a new
552-member Supreme Soviet. Unlike the
existing Supreme Soviet, which rubber-
stamps party wishes, the new body is
supposed to have real power and meet
eight months a year. Gorbachev is al-
most certain to be its president. But
since no one knows how it will work,
some Moscow insiders are already debat-
ing whether the legislature or the Com-
munist Party's Central Committee will
have a stronger say in making or defeat-
ing reformist plans.

GATHERING STORM. What is certain is
that heated debate lies ahead. Most can-
didates championed bread-and-butter is-
sues, but some strayed into dangerous
territory. Yeltsin, for instance, ran
against the party's privileged elite and
scored 89% of the vote in his Moscow
district. For some, he seemed to embody
popular distaste for the entire Soviet
system. More than a few voters told
Western questioners that he could be an
alternative to Gorbachev.

The political tempest will grow louder
in the coming weeks, as runoff elections
are held in districts where no candidate
won a majority or where unopposed can-
didates' names were inked out on the
ballot. The Academy of Sciences, for ex-
ample, must pick new candidates, be-

cause the scientists rejected the entire
slate after physicist and human rights
activist Andrei Sakharov was excluded.
Later, in the fall, a whole new series of
elections will be held for local and re-
gional legislatures.

As Soviets get used to exercising their
newfound political muscle, Gorbachev's
challenge will be to channel their dissent
into support for his programs. That will
mean persuading his citizenry to accept
higher prices, more competition, longer
workdays—and profits. Some Soviets
will grow richer than others. Unemploy-
ment is likely to mount, and inflationary
pressures will build.

The overarching question, of course, is
whether Mar. 26 marks the first step
toward weakening the Communist Par-
ty's once unassailable control over Sovi-
et society. By taking even the first steps
toward a more representative political
system, Gorbachev is encouraging direct
opposition to the party. And it may be
only a matter of time before budding
informal political and special-interest
groups push for more power-sharing—
or even a multiparty system. Then, final-
ly, would come the true test of Gorbach-
ev—the most fascinating and master-
ful leader his country has seen in many
decades.

*By Peter Galuszka in Moscow, with Rose
Brady in New York, Bill Javetski in Wash-
ington, and bureau reports*



OF SOVIETS WANT CHANGE. BUT HAVE THE ELECTIONS RAISED HOPES THAT EVEN GORBACHEV CAN'T MEET?

Commentary/by Sarah Miller

THE STRONG DEMAND FOR OIL MEANS ONLY ONE THING . . .

If you were about to panic over soaring oil prices, don't. When New York traders bid up futures contracts to \$20 a barrel and more, they were overreacting first to North Sea production outages and then to the Alaskan oil spill. Refiners, in fact, are paying far less for most of their crude oil. Indeed, relative sanity returned to the pits as soon as Port Valdez reopened

the oil industry did little better. Such thinking recalls the early 1980s, when the industry refused to admit that oil-price runups in the 1970s had throttled demand. Only now are oil-company economists gingerly coming around to the view that the price collapse of 1986 will goose demand (chart).

The evidence was there for those who chose to look. In real terms, oil prices today are near 1974 levels. And as in the late 1970s, says R. Bryan Jacoboski at PaineWebber Inc. in New York, economic growth and oil demand are rising almost in lockstep. Similarly, the cost of gasoline in the U.S., adjusted for inflation and automobile fuel efficiency, is at lows not seen since the

Iran, OPEC's traditional price hawk, succumbed to the lure of higher sales. Current estimates put Iranian production at 600,000 barrels a day over quota of 2.64 million.

THING OF THE PAST. But if OPEC sees content with current price levels, that hardly cause for rejoicing. For one thing, the first-quarter runup in oil prices will probably add 0.3% to the consumer price index over the course of three or four months, according to DRI/McGraw-Hill. Moreover, the profound deflationary benefits of falling oil quotes that offset price hikes elsewhere are now a thing of the past.

The outlook isn't much brighter for the trade deficit. U.S. oil demands

growing by some 2.5% a year, even as domestic production continues to slide. If the import bill swells even if prices remain stable. Industry experts reckon that domestic prices would have remained at more than \$20 a barrel for at least a year to reverse the decline in U.S. production, which plunged to 7 million barrels a day in 1988 from 18 million barrels in 1986. Should prices drop back to \$18 a barrel, predicts Jeffrey M. Browne, Amoco Corp. senior vice president for production, U.S. output will

to ships on Mar. 28. Still, you may have plenty of reasons to be worried. Growth in oil demand, coupled with signs of uncharacteristic discipline on the part of oil-producing countries, means that prices this year are likely to gyrate around a midpoint as much \$2 a barrel over last year's average. For the U.S., that portends continued inflationary pressure and slow progress in lowering the trade deficit.

GOOSING DEMAND. Rising oil demand, more than anything, is the culprit. It has been growing at a pace that has dumbfounded the supposed experts. As recently as November the International Energy Agency in Paris said demand in 1988 was growing at 1.7%. Its March report pegs 1988 growth at 2.6%. A similar upgrading of its 1.6% first-quarter growth estimate is rumored to be in the offing. Such a move would push the full-year 1989 growth forecast closer to 2%.

The bureaucrats in Paris weren't alone in missing this dramatic turn in the market: Most of their brethren in

1930s. Yet many oil economists still marvel that gasoline consumption is leading the growth in oil demand.

Luckily for oil consumers, OPEC producers seem to have a better grasp of the price-demand relationship. So the Persian Gulf nations are cranking up production rather than trying to force prices even higher by keeping their wares off the market. Kuwaiti Oil Minister Ali Khalifa al-Sabah in late March called for a second-half increase in OPEC's nominal production ceiling of 18.5 million barrels a day to 20 million barrels a day—about the level of real OPEC output so far this year. Even

OIL PRICES CLIMB BACK



fall a further 20% by 1995.

Add to that the prospect of flat or declining production in such non-OPEC areas as the British North Sea, and it's easy to figure that OPEC's control over the oil market can only increase. Former Saudi Oil Minister Ahmed Zaki Yamani, for one, estimates that Persian Gulf producers will account for 75% of the world's oil exports in the mid-1990s, compared with 45% today, giving the countries effective control over prices. With a little luck, they won't forget the lessons of the 1970s and early 1980s. But that's not exactly the sort of luck one likes to count on.



DREXEL WITHHELD MILKEN'S 1988 COMPENSATION, ESTIMATED AT \$200 MILLION

THE U.S. VS. MILKEN: HOW THE LAST ACT BEGINS

He could face 20 years in jail and \$5.5 billion in fines and forfeitures

From the outset of the government's probe of Wall Street wrongdoing, it's been obvious the prize target is Michael R. Milken, Drexel Burnham Lambert Inc.'s junk-bond chief. On Mar. 1, a federal grand jury filed a conspiracy, fraud, and racketeering indictment against him, his brother Lowell, and Bruce L. Newberg, a former Drexel trader who worked for Milken. Fines and forfeitures could total over \$5.5 billion. Milken alone faces 98 counts. Jail time could total 20 years. The Milken is to plead innocent. Newberg's plans are not immediately known.

The indictment mirrors a complaint filed last September by the Securities & Exchange Commission against Drexel and Milken. The government's goal, defense sources and former prosecutors believe, has been to put Milken out of business. Its tactics have been hardball: humiliate Milken, to force close associates to turn against him, to get Drexel to stop supporting him and cut its own ties, and to debilitate Milken's junk-bond operation in Beverly Hills. Prosecutors will hope, these sources speculate, that Milken will agree to plead guilty to criminal violations, pay a substantial penalty, and accept banishment from the Street. Finally, the government would like to undermine Milken's network enough so that it could never again engage in the illegal acts the government be-

lieves have been its *raison d'être*.

So far the success of the government's assault has been mixed. After the SEC filed its complaint, lawyers for Milken and Drexel concluded that most of the case was shaky. It depended largely on testimony by jailed arbitrator Ivan F. Boesky, whose allegedly illegal trading scheme with Milken was at the heart of the case. Documentary evidence of the arrangement appeared to them to be circumstantial at best.

Since then, the government has gotten several key Drexel employees to provide evidence to the grand jury. They include Cary J. Mautasch, a trader in New York who handled several of the allegedly illegal trades, and James Dahl, a star bond salesman with wide knowledge about how Milken's network operates.

DISMAL RESULTS. Yet it remains unclear how helpful these individuals have been. Mautasch, says a knowledgeable defense source, testified he knew of some of the Boesky trades but was unaware

There is no sign
that Milken is willing
to make a deal
with the government

of any Boesky-Milken arrangement. Prior to the SEC complaint, the grand jury also heard testimony from Charles Thurnher, who might have been very damaging to Milken. According to the SEC, Thurnher kept financial records of the arrangement. But defense sources say that Thurnher's testimony wasn't detrimental to Drexel or Milken.

Defense attorneys say prosecutors hoped the tax-fraud case against Bruce Newberg and employees of Princeton/Newport Partners, a small investment firm indicted last August for tax fraud, would be a potent weapon. The Milken indictment includes several Princeton/Newport-related counts. Yet despite intense cajoling by the feds, the defendants and Newberg, who handled Princeton/Newport for Drexel, have not provided testimony against Milken.

Yet prosecutors did win a jury conviction on Mar. 22 of Lisa Jones, who worked for Newberg. The jury found she had lied to a grand jury in denying knowledge of the tax-fraud scheme. Some defense sources speculate that the feds hope her conviction will convince Newberg to testify against Milken.

The prosecutors' biggest victory, of course, was convincing Drexel to agree to plead guilty to six felony counts last December. The government said Drexel caved in after it showed the firm incriminating evidence of wrongdoing by its employees. Sources close to Drexel claim the evidence was "not substantive" and did not relate to the Boesky-Milken arrangement. Drexel has said it acted solely to avoid a potentially ruinous racketeering indictment. At prosecutors' insistence, Drexel agreed to fire Milken and withhold his compensation for 1988, said to total around \$200 million.

ON LEAVE. But the plea agreement is contingent on Drexel working out a settlement of the SEC's charges. Those negotiations, however, are at an impasse. The SEC backed down from its original demand that Drexel move the junk-bond department back to New York, which some sources believe would have caused its virtual dismemberment. But the SEC refused to budge from a demand that Drexel fire Milken even before a settlement was negotiated. The main reason the indictment is being brought now, say lawyers involved in the negotiations, is to resolve the issue. Drexel will now put Milken on a leave of absence.

Despite all of this pressure, there is no sign that Milken or his brother will make a deal with the government. In the view of attorneys sympathetic both to the prosecution and defense, that is as it should be. As perhaps the most important legal assault against Wall Street in decades, the Milken indictment deserves to be resolved by a hard-fought trial.

By Chris Welles in New York

AIRLINES

WHAT COULD STALL A RUN ON NORTHWEST

Financial and regulatory hurdles might make a raider think twice

It seemed to be the case of the Masked Raider. On Mar. 28, NWA Inc., the parent of Northwest Airlines, announced that an investor holding 4.9% of its stock wanted to discuss a leveraged buyout. Wall Street eagerly churned up rumors about the raider's identity—Irwin L. Jacobs, Coniston Partners, Marvin Davis were all mentioned—and NWA stock jumped 9 points, to 70. By the end of the next day, however, no buyout artist had emerged from the shadows, and the stock closed down 1%.

RICH ASSETS. Northwest's announcement was the first tangible evidence that the takeover rumors dogging the company could be true. Northwest's stock has climbed steadily from 50 last October, and it has drifted up and down between 60 and 70 in recent weeks. Yet despite all that market interest, some cold, hard facts suggest that a Northwest takeover might not be that simple.

The airline's allure isn't hard to fathom. Both analysts and Northwest investors reckon its true asset value lies around \$100 a share. And after managing a difficult merger with Republic Airlines, Northwest Chairman Steven G. Rothmeier runs a thriving company with rich assets. Northwest's pretax operating earnings last year edged up to \$205 million on sales of \$5.6 billion. It has a lucrative system of routes to Tokyo and other Asian cities. It dominates hubs at Minneapolis, Detroit, and Memphis. Cash flow is strong, and debt is low (charts).

Even more intriguing are the company's Tokyo properties, which include a compound for employees, an office building, and a house for the general manager of the Pacific division. Last year a Japanese investment group, Koshin Corp., offered \$350 million for some of those parcels, but Northwest turned it down. "We tried everything possible to

get them to sit down with us," says Paul R. Alanis of Koar Inc., a Los Angeles real estate firm that worked with Koshin. Airline analysts believe that Northwest had figured the taxes on the sale were prohibitively high.

The Tokyo real estate, though, is probably the only asset that could be detached from the airline without hurting its operations. About 65% of NWA's estimated 1989 operating income of \$277 million should come from the Pacific operation. "If you took away the Pacific division," says Edmund Greenslet, an analyst who publishes *The Airline Monitor*, "then you have a system that doesn't dominate any big population center."

There's also Washington to worry about. Now that the Justice Dept. has announced that it will subject new airline deals to antitrust scrutiny, any buyout plan that relies on selling off choice pieces of Northwest's routes could be in serious jeopardy.

Given those hurdles, it's no wonder investors haven't bid Northwest up fur-

ther. "There is a value of \$100 a share there," says Karen Firestone, a fund manager at Fidelity Management in Boston, "but it would be difficult for a buyer to make a deal work at anything much more than the current price."

BUYOUT BURDENS. The skepticism about Northwest shows the general problem these days with treating airlines as takeover stocks. After a decade of takeovers and slugfests in fare wars, industry survivors such as United, American, Delta are piling up cash and increasing their earnings rapidly. The airlines still own many of their planes, which could be sold and leased back for even more money. Often their stocks trade for modest multiples. In short, airlines seem to have many of the characteristics that takeover specialists love.

But the airlines still have plenty of problems. Many carriers carry lots of plane leases that don't appear on the balance sheets—an extra cost that burdens any buyout. And unlike, say, a cigarette manufacturer, the major airlines have to acquire billions of dollars worth of equipment to stay competitive. Northwest, whose average plane is about 10 years old, has 139 planes on order. Whether the airlines buy or lease new aircraft, the costs will be high.

It's easy to see how the airlines could argue against leveraged takeovers. They can they appease institutional shareholders, who have had a taste of what airline stock can do when rumors go afire? "I think Northwest could pay a single big dividend, then pay a high regular dividend," says Michael Messner, a vice-president of Pioneer Management Co., which holds 1.3 million Northwest shares. If Messner's view gains support, the airlines may spend a lot more to keep their independence.

By Christopher Power in New York and Russell Mitchell in Minneapolis



BIOTECHNOLOGY

AT BOSTON UNIVERSITY, BIOTECH 101 IS NO BREEZE

Its \$47 million investment in Seragen isn't going to pay off anytime soon

Biotech companies that are slow to live up to their initial promise are a dime a dozen. But Seragen Inc. has an unusual majority owner: Boston University. Eager to profit on biotech, BU in August, 1987, paid \$25 million for control of Seragen, based in Hopkinton, Mass. Since then it has put up \$22 million more. But revenue-generating products are still nowhere in sight. Now the

school is looking for a way to cash out. Says a former Seragen rival: "BU just got to get out of an embarrassment."

BU first got involved in 1980 when it helped fund a consortium of scientists, including BU researchers. In 1984 the consortium's backers brought in Nycomed, a Norwegian conglomerate. In 1987, Nycomed wanted out, and BU stepped up \$25 million for Nycomed's inter-

That put BU's stake at about 76%. What got BU so excited? Seragen was suing the creation of a new class of enzymes through genetic engineering to fight cancer and other diseases. The technology had been developed in the university's medical labs by John R. Murphy, a BU biochemist and Seragen's chief scientist. Working with the diphtheria toxin, Murphy found a way to attach molecules that would bind with specific cell membranes. The work received a patent in June, 1987.

Murphy rushed into such a risky venture because, like many investors at the top of the market, it hoped to sell out quickly. In this case, through a public offering, says Charles W. Smith, Seragen's chairman and BU's treasurer. But just months later the stock market crashed—and so did the IPO market. At its core, product development has been slower and more costly than BU expected. Plus, Seragen built a drug-production plant before it had even submitted a single new-drug application to the Food & Drug Administration. It also laid off staff and shelved out for frills like phones. By November, 1988, annual expenses had ballooned to \$12 million.

TAKERS. Now, BU is looking for a corporate partner to help Seragen fund \$40 million that it could cost to bring drugs to market, according to Boston venture capitalists. But so far, no takers. BU denies that the company is for sale, but says it is in negotiation with potential partners, including Switzerland's Sandoz Pharmaceuticals Corp.

Now Seragen may be making some progress. In January the FDA approved clinical trials for Seragen's genetically engineered substance to treat leukemia and lymphoma. And two more are ready for tests on other cancers. "The company has superb science, no question about that," says Steven Lee, a Shawmut National Bank venture capitalist. "What's in doubt is whether a commercially viable product stream can be developed soon enough to get a decent return."

Here's another question: Should a university take such a gamble in the first place? Other schools have let go of research developed on campus rather than avoid potential conflicts. Notably, Harvard University refused to fund Genentech. BU President John R. Silber says that out of its \$110 million operating budget, the university is prepared to add \$13 million on Seragen annually for the next four years. "It will be a significant achievement for this university," he says. "What is inappropriate about bringing in some research with prospect in nine years of having a company worth millions?" Only the possibility of owning a company that's worth less than what you put in.

By Laura Jereski in Boston

BANKING

WHY ROBERT ABBOUD WANTS MCORP IN HIS CORRAL

Merging the ailing bank with First City would give him Texas-size clout

After months of struggle, MCorp only sinks deeper into quicksand. Days before a Federal Deposit Insurance Corp. deadline for would-be buyers for the ailing Dallas bank holding company, three small bondholders move to liquidate it. Then, several MBanks run out of funds, and on Mar. 29 regulators declare all but five MBanks insolvent. The 20 banks, with \$15.4 billion in assets, are now under FDIC management. The move ends Chairman Gene H. Bishop's six-month battle to recapitalize MCorp himself—and further muddles

his partners the title to First City, along with \$970 million in federal aid. First City's bondholders demanded more cash—and almost scuttled the deal. With foreclosures running at record levels in every major Texas city, analysts tittered when Abboud crowed that he would make 0.85% on assets in his first year.

No one's laughing now. First City unloaded more than 40% of its \$8 billion in loans to an affiliate for liquidation. Vice-Chairman Frank C. Cihak tightened credit reviews. And Abboud slashed overhead from 7% of assets to 3.6%, just above the U.S. average. The "bad" bank is collecting 137% of book value on the bad loans—while the "good" bank's 12-month earnings will near \$98 million. "We're right on the button," says Abboud. His first-year ROA reached 0.84%, and First City's stock shot up to more than 29 from 22½ in July.

BIG FISH. Weak spots remain. Consumer loans are slack: Nearly one-quarter of First City's loan growth came from leveraged buyout loans. And other recapitalized Texas banks, such as NCNB Texas National Bank, dwarf First City and might bid for parts of MCorp. As his rivals regain their footing, Abboud knows he must get bigger—fast.

Despite MCorp's estimated \$903 million loss in 1988, it retains a strong franchise in Dallas, where First City is weak. Together, they could save up to \$500 million a year in overhead. And financing a deal that size, around \$800 million, is "no problem." Says Abboud: "We're bombarded with people" with money.

But regulators may not want to give Abboud another hefty chunk of aid to buy a second troubled bank. The FDIC owns about 18% of First City, though Abboud says he's ready to buy it out. And the FDIC has other possible bidders, such as Kohlberg Kravis Roberts, former United Technologies Chairman Harry J. Gray and Chicago's Pritzkers, and Shearson Lehman Hutton. Also, bondholders will fight for the \$400 million left in MCorp's holding company.

Most of all, First City has to keep posting operating improvements. Abboud has every reason to do so: He and Cihak own almost 20% of the stock. "We're not going to do any dumb deals," Abboud vows. But in chasing growth, he has to make sure he doesn't stray too far into the sinkhole of bad Texas loans.

By Todd Vogel in Houston



ABBOUD: WILL A BIGGER BANK BE BETTER?

the protracted battle for the last big Texas-owned bank.

But a brash new player in Texas banking is raring to have a go at his Dallas neighbor. Fresh from a successful first year at his own troubled Houston bank, First City Bancorp, A. Robert Abboud wants to build a Texas money-center bank that's nearly twice as big. And MCorp would give him the deposit base he craves. "We would be derelict" not to consider a bid, he told BUSINESS WEEK.

Abboud is no stranger to ambitious undertakings. His hard-charging style got him bounced out of the chairman's slot at First Chicago Corp. But that same energy last April won for him and

ALMOST EVERYONE IS LISTENING IN ON THE TELEPHONE TALKS

A rich contract at AT&T might encourage unions—and fuel inflation

When American Telephone & Telegraph Co. and the Baby Bells last signed labor contracts in 1986, the industry was still reeling from the phone company's breakup. As a result, the unions settled for modest deals from the companies.

Now those contracts are expiring, and for the unions, transition time is over. The job losses that plagued the industry three years ago have all but ended, and union members want more of the high profits that most companies are enjoying. "Our objective is to make up for what we lost in the past three years and to improve ourselves over inflation for the next three years," says Morton Bahr, president of the Communications Workers of America (CWA).

DETERMINED. The companies still feel threatened by the new competitive environment, however. Union and company leaders have been rebuilding the cooperative relationship they had forged before a 17-day strike in 1986, but management remains determined to hold the line on costs. The negotiations that start at AT&T on Apr. 5 could be as difficult as the last time around. "We still need to bring down the cost of competition," says Raymond E. Williams, AT&T's vice-president for labor relations. "We're over market" in terms of labor costs.

The talks also may have repercussions outside of telecommunications. The 550,000 union members employed at AT&T and the Baby Bells are the largest labor group up for bargaining this year. A rich contract may encourage other unions—and unnervе markets already jittery over inflation.

The industry's big test will come at AT&T, whose contract expires on May 27. The CWA and the International Brotherhood of Electrical Workers (IBEW), which also represents telephone employees, hope to set a benchmark that they can press on the seven regional operating companies, whose contracts end two months later. In 1986 the unions gave up their cost-of-living adjustment (COLA), which had given them about 80% of any increase in the consumer price index

(CPI). They also accepted profit-sharing and onetime payments instead of percentage wage hikes. As a result, Bahr figures, union members' pay has trailed the CPI since 1986 by 3% to 4%.

In addition to making up for lost ground, the unions want pay hikes that at least keep them even with an anticipated inflation rate of 5% or so a year. Officials argue that the companies can



afford bigger raises because of the significant productivity gains they've made in recent years, which have come in part through layoffs of union members. Management is likely to push for a continuation of onetime payments in lieu of percentage increases. And, Williams says, AT&T doesn't want to reinstitute COLA.

The wild card is health care. The

'We've built a Cadillac health plan, and I'll resist any move . . . to reduce it,' says the CWA's Bahr

unions adopted cost-containment measures a few years ago, and they won't budge for a while. But now double-digit inflation has come roaring back. AT&T wants to shift some of the burden to employees. The unions see this as a matter of principle, however. "We've built a Cadillac health plan for our members, and I'll resist any move, even in a month, to reduce it," says Bahr.

BROWNIE POINTS. But health care could be the key to a compromise on the all issue of pay. If management decides that it can forgo health care cost-sharing, union officials say that they will probably accept a lower wage package. "If health care is an issue for us, COLA is for the union, we need to work this out somehow," says Williams.

The unions hope their cordial relations with management will carry them to the bargaining table. Bahr and John J. Barry, the IBEW's president, meet regularly with Williams and Robert E. Allen, AT&T's chief executive officer. The unions have earned brownie points by helping the companies in Washington. In mid-March, the Federal Communications Commission agreed to regulate AT&T through price caps rather than its rate of return, giving the company a potentially huge earnings bonanza. AT&T officials acknowledge that CWA lobbying support was key to getting Congress to go along with the move.

Union officials say they're determined to avoid another disruptive strike—chiefly because highly automated AT&T can keep services running during a walkout. So the unions are cashing in about for novel ways to put pressure on AT&T. The Canadian telecommunications union experimented with several new ideas, such as jamming Bell Canada corporate phone lines, during a recent strike. Now the CWA is trying to come up with more such tactics. "We plan to have a program that escalates during negotiations, so that the company will have an incentive to settle," says Bahr. Although such disruptions could expose the union to legal risks, he plans to try them anyway.

If telecommunications workers win healthy pay hikes that put them ahead of the cost of living, they would be one of the first union groups to do so in years. That would be good news for other unions. But to economists, it would be another unwelcome sign that inflation is heating up again.

By Aaron Bernstein in New York and Susan Garland in Washington



CEO BASS: COOPER'S LEGAL PROBLEMS "COULD SCARE THE CAPE OFF SUPERMAN"

AN ARTHUR BASS HOUSE COOPER FROM ITS SICKBED?

ring the health care outfit's ills may be harder than launching FedEx

The crayons that the trendy Palo Alto (Calif.) eatery MacArthur Park stacks on every table make it Arthur C. Bass's kind of place. "Business is chess, not checkers—a matrix of at-ifs," Bass says as he begins talking on his place mat. He draws a map of how a well-positioned company must exploit such social forces as the aging population, the national debt, the drug epidemic, and ecological concerns. A successful company, a "moon shot," continues, is one that taps into those forces. Look at Federal Express Corp., the huge overnight shipper he helped found and run. Now, Bass is preparing a shot at the moon: The Cooper Cos. **STRATEGIC VISION.** Go ahead and snicker, but the saga of this health care outfit about to take another odd turn. Bass, who in March was tagged as Cooper's chief, hopes within a month to win board approval for his 30-page "strategic vision." Assuming he does, this summer he and a core team of marketers and researchers will move to New York. There, Bass's team will begin drawing a cash hoard that could range upward of \$225 million. He's confident, to the least: "I create picture-book companies out of crap," he boasts. Size isn't

his goal, but Bass expects the cash could "lever us into a \$2 billion deal."

It takes a lot to surprise Cooper-watchers. But Bass may do the trick. And on Mar. 28, Cooper delivered another eye-opener: Frederick R. Adler, the noted New York venture capitalist, has joined the board. "Art's thought process and Fred's deal flow," Houston investor Ronald A. Lerner says, should mean "a dynamite combination."

Indeed, getting Adler on board looks like a coup for the two trios of brothers, the Sturmans and the Singers, who last July wrested control of Cooper from founder Parker G. Montgomery. Once a maker of well respected lines of contact lenses, ophthalmic supplies, and surgical products, Cooper was driven to the brink of insolvency by high overhead and Montgomery's runaway dealmaking.

The rookie raiders, who made their money in New York real estate, weren't left with much. The brothers barely stayed off bankruptcy last fall. To their credit, they've agreed to sell nearly \$1 billion worth of Cooper assets. But sources close to Cooper say that they remain perplexed about just what to do with the remains of their prize.

Choosing Bass, says one source close

to the board, was a means of resolving a four-month "chicken-and-egg" debate over whether they needed a generalist to set a strategy or a specialist to execute one set by outside consultants. The first view prevailed. "Art will be running a venture fund here soon," says Cooper's only outside director, Rorer Pharmaceutical Corp. President Ralph H. Thurman. "He's got the vision, intellect, and creativity to do that."

Whatever else you can say about him, Bass's background is certainly eclectic. As FedEx stumbled in the mid-1970s, Bass helped set it right, serving as president and, eventually, vice-chairman. "Art was the guy who held it all together," says Frank Maguire, former senior vice-president of Federal.

But Bass tired of FedEx's bureaucracy and by 1982 had left to join Midway Airlines Inc. There he focused on improving operations. He bolstered Midway's sagging image by selling business travelers on a way to avoid Chicago's O'Hare International Airport. Midway's board grew impatient with the company's slow financial rebound, however, and ousted Bass in 1985. Most observers still credit him with laying a foundation for Midway's later turnaround.

Bass should shake up Cooper. "I believe in contentious management," he says. "Somebody should be able to walk in and call me a jerk as long as when we leave the room we're all on the same wavelength." Do the Sturmans and Singers agree? "I don't think so," he allows.

FAT PAYCHECKS. The most critical hurdle ahead is closing the sales of the remaining businesses, especially the Technicon division, a medical-testing-device maker in Tarrytown, N. Y. It's set for sale to Miles Inc., but the deal must be approved at a shareholder meeting in May. Selling Technicon will wipe about \$260 million of Cooper's hefty \$630 million debt off its balance sheet and give the company another \$212 million in cash.

What's more, Cooper "is fraught with litigation concerns that could scare the cape off Superman," says Bass. Several investors are suing. They remain upset at the generous paychecks the families get, including total salaries of \$1.2 million for five of the brothers, plus \$200,000 for Martin Singer, father of three directors, as a "special consultant." Sputters one shareholder, who says he's pondering a lawsuit himself: "The compensation is just outrageous."

Bass says he's "more penurious" than that, which should help him with shareholders, who last year saw Cooper lose \$152 million on sales of \$611 million. But before the stock heads north from its current level around \$4, investors will demand more than a good track record and a Crayola sketch of the future.

By Joan O'C. Hamilton in Palo Alto, Calif.

TAKEOVERS



MIAMI'S CARLYLE HOTEL: PELULLO'S OFFICE IS ART DECO, BUT HIS BID FOR DWG IS BAROQUE

VICTOR POSNER MAY SOON TASTE HIS OWN MEDICINE

The tangled tale of how the raider's DWG got put into play

In his office atop the Carlyle Hotel in Miami Beach's Art Deco district, Leonard A. Pelullo has been pondering what went wrong with a recent \$572 million bid for DWG Corp. Five miles north along Collins Avenue in the offices of Victor Posner Cos., DWG directors met on Mar. 28 to ponder the same thing.

Miami Beach is surely a strange setting for a takeover play. But this tale, bizarre as they come, deserves it. Posner, his onetime consultant, Pelullo, and Pelullo's New York lawyer, Andrew N. Heine, have Wall Street all confused.

If you had been following the news, you would be scratching your head, too: Last fall, at Posner's behest, Pelullo urged Heine to bid for Posner's electrical contractor, Fischbach Corp. Heine did, and takeover talks appeared to go on until March—when Heine abruptly dropped the bid and instead offered to buy DWG, keeper of the Posner empire's crown jewels, Royal Crown Cola and Arby's Inc.

Posner's response? Get lost. The upshot is that what started out as perhaps too-chummy talks toward a friendly deal suddenly became a full-scale takeover war—one in which the end is far from clear. While neither Posner nor his asso-

ciates are talking openly, that's the picture that emerges from a review of securities & Exchange Commission filings and extensive interviews with Pelullo, Heine, and dozens of other sources.

Victor Posner, 71, is no stranger to controversy. He built his \$2 billion-plus empire atop a mountain of debt, and mined it for a lavish salary. Last year from DWG alone he earned \$3.5 million—and perks. Posner's companies, on the other hand, haven't always fared so well, and by 1987 he was scrambling from creditors who were after his Sharon Steel Corp.

Enter Pelullo. The 38-year-old chairman of Royale Group Ltd. has mostly tried to keep alive a string of Art Deco hotels in south Miami Beach. Creditors are threatening to foreclose on them. He describes himself as a "work-out" specialist, a savior of companies endangered by too many creditors. Sharon seemed like a natural, so in October, 1987, he told Posner he would like to buy it. Posner said no, but added: Why don't you work for me as a consultant?

He did, and in Posner circles Pelullo soon came to be

known as Bob Paris. Why? Pelullo wanted to avoid drawing attention to a 1985 New Jersey State Commission Investigation report on boxing that mentioned him as "a key organized crime associate from Philadelphia." He does any ties to the mob.

EARNED FEES. In any case, his consulting task was to keep for Posner as much control of Sharon as possible. That effort failed. Two months after Pelullo started work, the bankruptcy court appointed a trustee to run Sharon. Posner kept Pelullo, who through June got \$1.2 million in consulting fees from DWG.

That didn't sit right with Mitchell Gregory, a DWG financial vice-president. "I didn't see anything of tangibility that had been done for that money," Gregory says. When Gregory raised the issue with the DWG board's audit committee, he was fired, he says. Director Thomas A. Prendergast would discuss Gregory, but he says the comments were for the Sharon Steel job.

dismisses queries about why DWG made them and not Sharon. Prendergast further notes that auditors reviewed the payments. DWG's auditor, Arthur Andersen & Co., won't comment. Pelullo insists he earned his fees, but discloses few details on how.

Pelullo readily acknowledges that a couple of months after getting the \$1.2 million, he hit up Heine, an old friend, to buy Fischbach. So Posner bought it in 1985, a soft market for the sort of big utility projects Fischbach works on had slashed prices. Worse, the SEC last year sued Posner and his son Steven on charges that he took over Fischbach by trading stock illegally. The suit is pending, and the Posners have denied any wrongdoing.

Fischbach wouldn't have been Heine's first takeover. He engineered a buyout of Kinney Systems Inc., the parking lot operator he now heads. So Sept. 29, when Heine offered \$25 a share for Fischbach, Wall Street bit, sending the shares up to 20. Heine says that he met with Posner the times. But sources on the sides of the deal say it broke down in January, with



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work, talked. If, as Heine planned, Fischbach were to sell its real estate to DWG, the deal would be a success. Fischbach's work, AIG won't comment. Fischbach now trades for less than 16¢.

Pelullo claims Posner associates. He says they were hired to prepare a bid for DWG. On Feb. 10, Pelullo says, the firm was told by the SEC that its bid was "not in the stock as low as 6¢. He arranged financing through Trafalgar Holdings Ltd., the firm set up by Charles Knapp, ex-head of the disastrous California thrift company Financial Corp. of America.

By Mar. 9, Pelullo and Heine were in the 101 Club. That morning, Pelullo had met with Posner's attorney, Martin Rosen. He came away convinced that Posner would be enticed by a bid of \$22 a share—potentially a steal, since DWG's various assets, which also include propane and textiles, have been valued at up to \$33 a share. "I think it's a great company," Pelullo notes. "It's undervalued."

NO SALE

Why was Posner selling? Had he at last been beaten down by his court battles, or was he looking for a way to settle the SEC's suit? Wrong on all counts. Indeed, Pelullo and Heine learned only hours after their celebratory lunch that Posner wouldn't sell. "I was shocked," Pelullo says.

No wonder. A top partner in the law firm of Underberg, Manley, Myerson & Casey, Heine had seen that firm wind up in Chapter 11. If his bid for DWG sputtered, he could kiss his credibility on Wall Street goodbye. So he decided to fight publicly for DWG. On Mar. 24, Heine said that he would sue in Ohio, where DWG is incorporated, to force a vote of disinterested shareholders on his offer.

On Heine's bid, investors sent DWG up to 16¢. But the American Stock Exchange is tracking suspicious trading in DWG. In any case, Wall Street can't figure out which way to go—up toward the bid or down around 7¢. Some investors are skeptical of Trafalgar's ability to finance a deal. Moreover, "if you really love your house, you won't sell, no matter how much someone offers," says one investor.

wanted guests. Pelullo and Heine don't

By Gail DeGeorge in Miami

THE BOTTOM LINE: GRAMM-RUDMAN ISN'T WORKING

There are two kinds of currency in Washington these days, real money and Gramm-Rudman money. Real money is what the government prints, borrows, taxes, and spends. It pays for an F-15 fighter or the salary of a government health inspector. Gramm-Rudman money, on the other hand, is the way Congress and the Administration score their annual budget game.

Passed in 1985 to force Congress to meet annual deficit targets, the Gramm-Rudman Act succeeded in its first year. But since then, it has become an excuse for accounting gimmickry and economic sophistry. For the past three years, Congress has seemed to meet the statute's budget targets. Yet the real-world deficit has remained virtually unchanged. "We have developed considerable skill and sophistication in meeting deficit-reduction targets—without reducing the deficit," says Joint Economic Committee Chairman Lee H. Hamilton (D-Ind.).

'THE ONLY GAME.' Supporters insist that, for all its flaws, the balanced-budget law is better than the fiscal anarchy of the early 1980s. "It's the only game in town," says Senator Warren Rudman (R-N.H.). "Without it, we would be a lot worse off."

Maybe. But take the current debate over the thrift-industry bailout. In fiscal 1990, the government will have to borrow at least \$25 billion to shut down flat-broke thrifts. Yet if it accounts these costs in the budget, it would blow the Gramm-Rudman target out of the water.

So the Administration's green-eyed types came up with a way to get the money. First, they will borrow the money through a new quasi-government entity, rather than directly through the federal Treasury. That way, borrowing costs "off-budget," so they won't count against the Gramm-Rudman targets—a scheme that will cost taxpayers up to \$5 billion in added interest payments over the 30-year life of the debt. Bond proceeds,

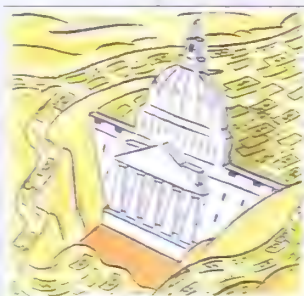
however, will count toward reducing the Gramm-Rudman budget shortfall. After all the paper is shuffled, the \$5 billion in new debt will show up as a total increase in the Gramm-Rudman goal of less than \$2 billion.

ENDLESS SQUABBLE. Consider another trick. Lawmakers could meet their fiscal 1990 deficit target by advancing Oct. 1 military payday by 24 hours. That would dump those expenses on the fiscal 1989 budget, which ends Sept. 30. No one would notice because the focus always is on the coming fiscal year. The government still must borrow the money, but in Gramm-Rudman land, that does matter.

Accounting gimmicks aren't the only problem. Congress' obsession with the phony target precludes serious debate on substantive issues. For example, President Bush's proposal to reduce capital-gains taxes has degenerated into an endless squabble over whether or not it will lose revenue. No one ever asks if it would be an efficient way to encourage capital investment.

There are solutions, however. Former Congressional Budget Office Director Rudolph G. Penner has one alternative. The separate House and Senate budget committees would be replaced by a single panel of congressional leaders. The President would sign off on Congress' budget parameters for the year. To maintain discipline, lawmakers would have to offset any new spending by cutting elsewhere in the budget. The artificial Gramm-Rudman goal, which creative accounting can render meaningless, would be replaced by more realistic procedures. The focus would shift to real tax and spending priorities.

Rudman once called the balanced-budget law "a bad idea whose time has come." That was probably true in 1985. But now, it turns out, the law's time has gone. There are no magic potions for reducing the deficit. Congress should face up to its constitutional responsibility to balance the nation's books honestly.





"I have to laugh when they call it a 'start-up' company."

"It's the only one that hasn't been split up, merged, or sold out. The same people who put it together still run it."

"Actually, they're the most stable company in the business."

—financial manager

MCI. We showed them. Let us show you.

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EDITED BY HARRIS COLLINGWOOD

JUSTICE CRACKS A COCAINE CARTEL

► The U.S. struck a blow against a powerful Colombian cocaine cartel. On Mar. 29 the Justice Dept. announced it had infiltrated the Medellin cartel's vast money-laundering operations, leading to the arrest of 127 individuals and the indictment of Colombian and Panamanian bank officials. The bankers admitted to undercover agents that they had laundered more than \$400 million in drug money, according to federal officials.

Government officials also are starting proceedings to seize millions of dollars from 16 U.S. banks, including Continental Illinois and Chemical, through which drug profits flowed. No criminal charges were filed against the U.S. institutions, which officials said cooperated in the two-year investigation. But the government is demanding that the banks repatriate money that went to overseas branches.

MINKOW GOES TO THE HOOSEGOW

► Barry Minkow, once Wall Street's darling, ran out of charisma on Mar. 27, when he was sentenced to 25 years in federal prison. In December, Minkow was convicted on 57 counts of fraud and conspiracy for charging insurance customers for phony carpet restoration work. He must also pay \$26 million in restitution.

Minkow, 23, built zzzz Best into a 21-office carpet-cleaning empire in three states before it collapsed in 1987. Prosecutors at his trial linked him to organized crime figures who steered bogus business to him.

GTE STRIKES BACK AGAINST RATE CUTS

► GTE knows Texas politics. Last month the state's Public Utilities Commission ordered

the phone giant to cut its rates in Texas by \$59 million and refund customers \$128 million in overcharges. On Mar. 28, GTE said it would lay off 600 workers in Texas, delay hiring 400 more, and rethink moving its telephone operations to Irving, a Dallas suburb.

Now, Texas legislators are demanding a reversal from the PUC. But GTE is probably just looking for a compromise. The company has spent millions planning its move to the Las Colinas corporate park, two-thirds of which remains undeveloped. And several hundred GTE workers out of a planned 3,000 have already moved. GTE can argue its case before the PUC on Apr. 5.

BABY BELLS AND POISON PILLS

► The megadeals of recent months have even the Baby Bells maneuvering to fend off corporate raiders. Philadelphia-based Bell Atlantic on Mar. 28 adopted a poison pill that kicks in when just 15% of the company is acquired.

That hair trigger hardly seems necessary, given Bell Atlantic's \$14.9 billion market capitalization and the regulatory bias against utility takeovers. Two other Baby Bells, Chicago-based Ameritech and Southwestern Bell of St. Louis, each have 20% thresholds in their plans. Whatever the

A BIRD IN THE HAND IS WORTH

Diane Claussen knows her boss, Larry Cahill, is a busy man. He's the president of Larkin, a motel developer and franchiser based in Cedar Rapids, Iowa, and she doesn't waste his time with frivolous matters. So when a cage containing a homing pigeon and addressed to Cahill arrived at the office, she hesitated before showing it to him.

Fortunately, Cahill accepted the odd package with good humor. Then he looked over to accompanying letter from Homewood Suites, an extended-stay hotel franchise whose marketing people figured Cahill was good prospect, if only they could get his attention. That he did. Following the letter's instructions, Cahill released the bird and called Homewood's development director. Now he's looking for just the right spot to build a Homewood Suites hotel.

Homewood marketing chief Jennifer Burgess is sold on the pigeon ploy. Her reasoning: "You just can't ignore a live bird."



limit, raiders and their allies are hopping mad. Says Ralph Whitworth of the United Shareholders Assn.: "All this does is set up a fortress around the management."

FRUEHAUF BUYS SOME TIME

► Fruehauf finally sold its struggling tractor-trailer and maritime divisions on Mar. 28, but the deal merely buys the Detroit company some breathing room. Management has tried for months to hack away at some \$710 million in long-term debt and \$100 million in annual interest payments. The debt is the legacy of a lever-

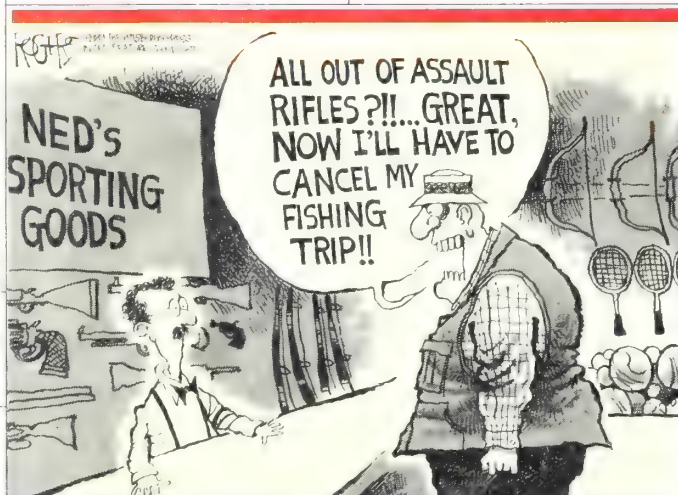
aged buyout the company undertook in 1986 to fend off raider Asher Edelman.

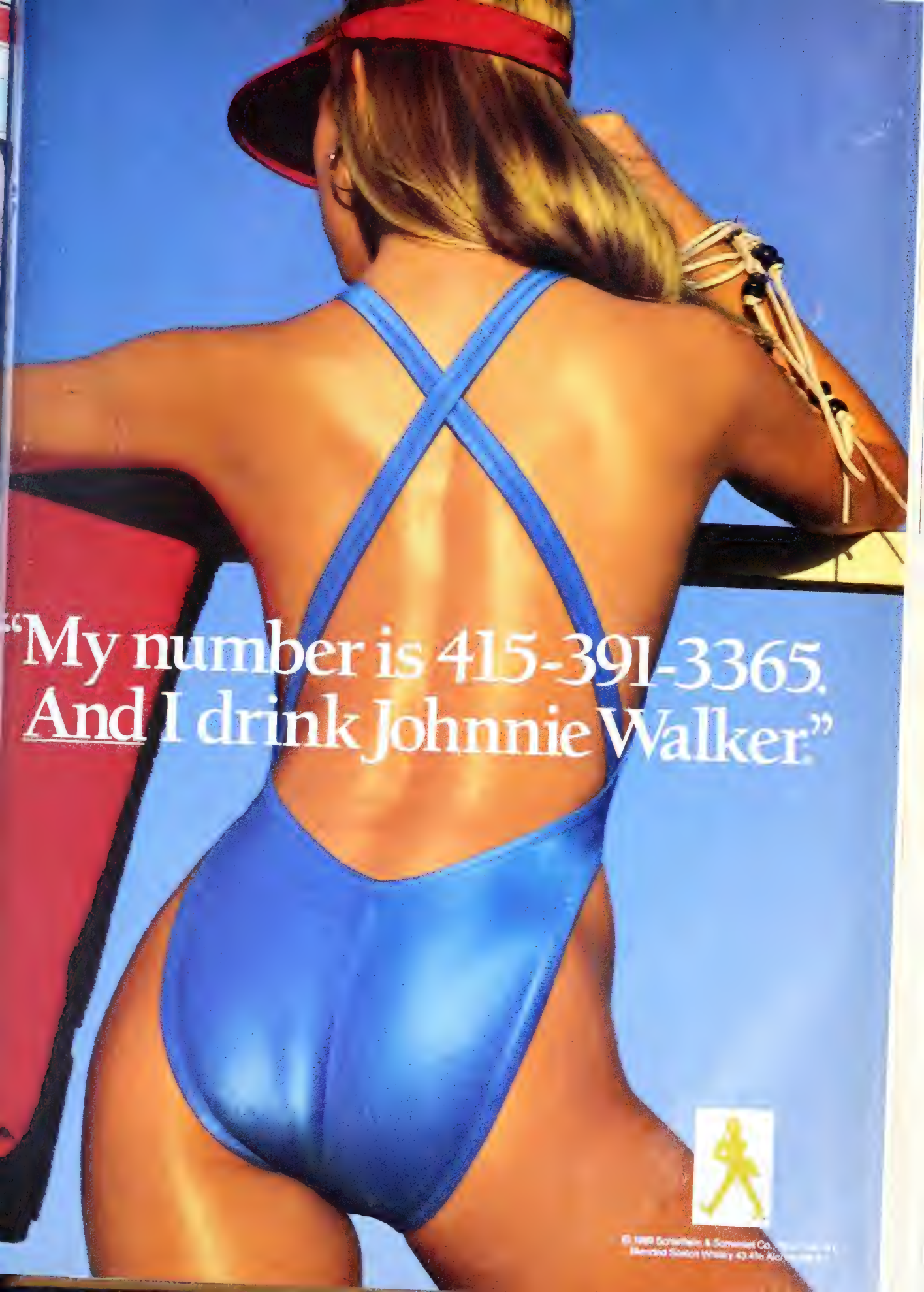
The \$233 million sale of Terex is a prelude to more drastic debt-reduction measures. The next likely step is the sale of auto-parts maker Kelsey-Hayes, the company's only profitable business. Analysts estimate that the division, which last year earned \$60 million, could fetch \$70 million to \$900 million.

THE SOVIETS GET BIG U.S. PARTNERS

► A six-company U.S. consortium plans to set up more than 25 joint ventures in the Soviet Union, giving a boost to Mikhail Gorbachev's drive to remake the Soviet economy and political system. An agreement was scheduled to be signed in the Kremlin on Mar. 30.

The consortium members are RJR Nabisco, Archer Daniels Midland, Eastman Kodak, Chevron, Johnson & Johnson, and Mercator, a merchant bank. Ford Motor, worried that the agreement did not go far enough in addressing the problems of doing business in a nonmarket economy, dropped out of the group before the signing.



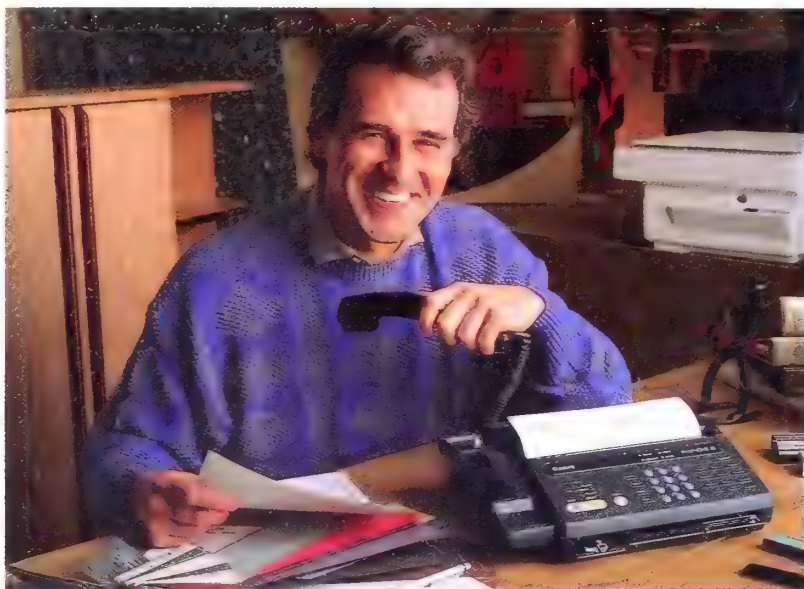
A woman with blonde hair, wearing a red visor and a blue one-piece swimsuit with a crisscross back, is seen from behind. She is holding a red surfboard under her left arm. The background is a clear blue sky.

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BUSH'S FIRST BIG CHANCE TO SCORE ENVIRONMENTAL POINTS

During the campaign, the environment was one of the few areas where George Bush distanced himself from Reagan's policies. Since the election, President Bush has made all the right symbolic moves to underscore his concern, from naming respected environmentalist William K. Reilly to head the Environmental Protection Agency to discharging top aides to a disastrous oil spill in Alaska.

Now Bush's environmental commitment is facing its first serious challenge over the controversial issue of fuel efficiency standards. Transportation Secretary Samuel H. Skinner is alarmed by Detroit's balking on fuel efficiency, growing U.S. dependence on imported oil, and pollution concerns. He is urging the White House to toughen the Corporate Average Fuel Economy (CAFE) standards that require auto makers' fleets to average 26.5 mpg. Detroit is balking.

Bush's decision, likely to be announced in early April, will be a sign of his willingness to go on powerful economic interests in the name of the environment. "This has a symbolic significance far beyond the specifics," says Nicholas A. Fedoruk, director of the Energy Conservation Coalition, a group of 20 organizations.

ITISH. Skinner wants to enforce an oft-delayed regulation cutting the gasoline mileage for all domestically produced cars an average of 27.5 mpg for each manufacturer. The most recent delay came last year, when then-Transportation Secretary James H. Burnley IV set the requirement at the current 26.5 mpg and proposed junking the CAFE standard altogether. Skinner came into office insisting that not "enough attention has been given to environmental issues and fuel economy." In March he urged Bush to adopt a tougher policy. Skinner has the backing of the EPA's Reilly and the Energy Dept. Still unclear is whether antiregulation forces at the Office of Management & Budget and skittish White House political aides will derail Skinner's plan.

Worried about smog and the possible global warming of the

earth's atmosphere due to carbon dioxide, many environmentalists say that stronger measures must be taken to curb fossil-fuel use. According to Transportation Dept. figures, hiking the CAFE standard by 1 mpg for two model years would reduce carbon dioxide emissions by 18 million tons over the lifetime of the cars. That's roughly equivalent to three weeks of carbon dioxide pollution in California.

Unless Bush acts, Congress might step in with far more drastic measures. Hill Democrats are mulling over a rise in the standard to as much as 30 mpg by the mid-1990s and 45 mpg by the turn of the century.

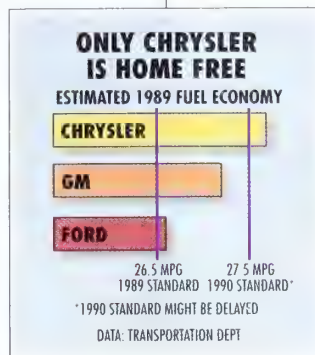
Still, even a modest boost by the Bush Administration would give Detroit heartburn. The industry says weight-reducing measures and better aerodynamics have improved mileage about as much as is technologically feasible. Detroit fears that more stringent mileage standards will collide with Americans' growing appetite for big cars. Due largely to increased demand for gas guzzlers, the fuel efficiency of Chrysler Corp.'s fleet is expected to average 27.7 mpg this year. That's down from 28.4 mpg last year. Ford Motor Co. peaked at 27 mpg in

1986 and may slip to 26.5 mpg this year. General Motors Corp. may average 27.2 this year, down from 27.6 in 1988. "You can't make people buy what they don't want," says Albert J. Slechter, Chrysler's government affairs director.

If CAFE rules are stiffened, the companies could eventually face big fines for violations. Ford once even threatened to move big-car production offshore to avoid the penalties, and it says it is keeping the option alive. Ford and Chrysler say a stiff gas tax would be a better way to cut fuel consumption.

The normally probusiness Bush may shrug off these arguments. Skinner's case is building momentum within the Administration. And Bush may be willing to take the heat from Detroit to gain some much-needed political mileage.

By Seth Payne and Vicky Cahan in Washington, with David Woodruff in Detroit



CAPITAL WRAPUP

LOBBYING

They say politics makes strange bedfellows. That doesn't stop when politics move into the business world. With the 1988 election fast becoming a distant memory, Boston advertising executive John Sasso, who ran Michael Dukakis' Presidential campaign, and Washington lobbyist Craig L. Fuller, a former top aide to George Bush, are teaming up to help the nation's auto insurance industry. The duo will be advising the Insurance Information Institute, which is planning a national ad campaign and an aggressive lobbying drive to combat moves to roll back automobile insurance rates in Califor-

nia and other states. Says Fuller of his association with Sasso: "We were on different sides last year, we're working together this year. But all bets are off for 1992."

POLITICS

There's a strong sense of déjà vu in a few of next year's Senate races. In Minnesota, former Vice-President Walter F. Mondale is considering a run against incumbent Republican Rudy Boschwitz for the seat Mondale held until 1976. Polls show Mondale with a lead. And in North Carolina former Governor Jim Hunt, who lost to GOP Senator Jesse Helms in a celebrated 1984 slugfest, is weighing a rematch.

PEOPLE

Environmental Protection Agency Administrator William K. Reilly is assembling his management team. Henry F. Habicht Jr., who headed an active environmental enforcement group at Justice during the Reagan Administration, is slated for the No. 2 slot. For policy chief, Reilly, a former head of the Conservation Foundation/World Wildlife Fund, chose Terry Davies, executive vice-president of the conservation group. And William J. Rosenberg, a Michigan real estate developer, lawyer, and close associate of Bush confidant Robert J. Teeter, was recently nominated as air-quality chief.

JAPAN BUILDS A NEW POWER BASE

ITS EMERGING CLOUT IN EAST ASIA COULD COME AT AMERICA'S EXPENSE



When Yeh Chih-Chien, now 30, was still in high school in Taiwan, he dreamed of studying in America. But his father sent him to Japan. Now, he says, as he happily starts work at Honda Motor Co.: "In auto engineering, Japan is No. 1."

Isariya Krongamphang, 27, studied French in high school in Bangkok but switched to Japanese in college. Now she's setting up a joint venture with a Japanese company to export frozen food to Japan: "The Japanese are doing more and more business here."

Philip Tsang, 29, has started a Hong Kong trading company to sell made-in-China baby clothing. Rather than try to crack the U.S., he's going after Japan. "Japan is a lucrative market," he says. "And it's just opening."

After decades of looking to America for economic growth, the nations of East Asia are undergoing a tidal change. Their economic focus is shifting toward Japan. This is letting Japan build a new power base that helps integrate Asian countries into its economic and diplomatic agenda.

It is happening despite deep and often painful memories of the Greater East Asia Co-Prosperity Sphere, Japan's name for its military occupation and economic exploitation of much of Asia at

the height of World War II. Instead of prosperity, Japan's empire brought misery to a region stretching from China to Southeast Asia and the South Pacific.

Today, the region's economy is the fastest growing on earth. Its industries spew forth cars, computers, microchips, and toys for the world. Not counting Japan, growth rates have averaged 8% for the past two years, reaching double digits last year in China, Thailand, South Korea, and Singapore. Per capita incomes have risen dramatically.

And Asians are determined to keep growing. They know that America, whether because of recession or protectionism, will be unable or unwilling to absorb further surges in Asian exports. They see U.S. companies exacting a high price for their technology rather than practically giving it away as they once did. U.S. foreign aid has been slashed, and U.S. multinationals have slowed their expansion. And a new worry has arisen: that the U.S.-Canadian free trade area and Europe's scheme to integrate its markets by 1992 could be used to lock Asians out.

'FULL-GROWN.' Small wonder, then, that Asia's leaders are scrambling to attract business, investment, and aid from the former colonizer. To stay in tune with Japan, the Taiwanese install tiny rooftop satellite dishes to receive Japanese television broadcasts. Singaporean tour guides are busy learning Japanese. Japanese consumers buy Taiwanese bicycles

**SIGNS OF THE TIMES:
JAPANESE COMPANIES
GET TOP BILLING
ON HONG KONG'S SKYLINE**



videocassette recorders imported in Korea. "A full-grown economic ere is evolving naturally among the ntries around Japan," says Masao ioka, president of the Manila-based an Development Bank.

s the economies of East Asia grow e dependent on each other, Japan is rtaking the U.S. as their largest for- n investor and aid donor. President rge Bush's February trip to Japan, na, and Korea did little to dispel s that America is falling behind in region. Although the U.S. is still the est export market for many coun- s and helps maintain the region's mly balance of power, Asians are not e it will last. "U.S. economic influ- e in Asia is still greater than Ja- s," says Singapore's Trade Minister, Hsien Loong. "However, if present ds continue, the influence of the Jap- se economy on Asia might equal or n surpass that of the U.S."

Japan's economic role in Asia has been building for years, but it has recently begun to expand rapidly. The world's largest aid donor, Japan now is handing out nearly \$7 billion a year in Asia. In contrast, U.S. military and economic aid to the region amounts to roughly \$500 million. Japanese investments there more than doubled in fiscal 1987-88. Driven by the strong yen, some Japanese companies have virtually transferred their manufacturing bases to such countries as Thailand. Japan is buying more from these countries, too: Its imports from the region rose by 68.6% from 1986 to 1988, compared with 31.5% for the U.S.

More than ever, the Japanese are groping for a political and diplomatic role in Asia commensurate with their economic clout. They are launching programs, organizations, and study groups to determine how they can become a decisive diplomatic player in Asia without offending their neighbors.

The Japanese use a poetic but self-serving metaphor to describe their emerging role in Asia: Japan is the lead bird in a formation of wild geese. All are flying forward as each picks up the industries sloughed off by the countries ahead of it. The newly industrialized economies such as Korea and Taiwan are racing to catch up with Japan, and the less developed Southeast Asian countries are following close behind.

Not all Asians are enthusiastic about this image. The idea of being dominated by a powerful Japan arouses deep anxiety. Chinese and Koreans in particular are resentful of Japan's occasional attempts to deny that its prior domination of Asia constituted aggression.

THE ONLY GAME. But no one wants to miss out on the wealth Japan is creating. In China, scholars are reacting in a surprising way to the notion of an East Asian economic sphere: Instead of worrying about Japanese domination, they fret that Tokyo is trying to exclude China. Indonesia and the Philippines have largely missed out on Japan's latest investment surge, and they want a piece of the action, too. "There is really no option here," says Narongchai Akrasanee, executive vice-president of the Thailand Development Research Institute. "If any Southeast Asian country wants to see economic growth and industrialization, this is the game it has to play, like it or not."

Despite closer economic ties within the

region, most Asians agree they should avoid creating a trading bloc that might become "Fortress Asia." There is a new pragmatism about doing business with Japan, but the Asians want to maintain U.S. links as a counterweight. "We want to see the world remain open and free," says Philip Yeo, chairman of Singapore's Economic Development Board. "To create little [regional] pockets is like going back to barter."

'CATCH-22.' Some U.S. critics say that Japan's economic and political emergence in Asia, combined with its increasing defense spending at home, represents a power grab. But it's not quite that simple. The U.S. has pushed Japan into a broader role, seeking Japanese help in maintaining the stability of the region at a time when U.S. resources are stretched. "It's catch-22," says Takujiro Hamada, a ruling-party member in the Diet. "The West wants Japan to cover the costs while leaving decision-making to others."

After years of helping Asia's economies grow, the U.S. is pressuring Japan to help absorb more Asian exports. And while cutting U.S. aid to the region, Washington has persuaded the Japanese to increase theirs. "One big question is how to keep our allies properly afloat when the U.S. has cut down its foreign aid enormously," says Robert J. Myers, president of the Carnegie Council on Ethics & International Affairs, which is launching a program to explore how the U.S. and Japan can cooperate to stimulate the Philippine economy.

If Americans can figure out a way to rely on Japanese wealth without sacrificing influence, so much the better. But Asians are beginning to wonder whether the U.S. might simply get left out in the "Pacific Century."

For years, Americans have been enamored of building economic ties with the Pacific Rim, believing that it would help the U.S. economy to sustain growth. But the Pacific Rim concept is getting stiff competition from a new approach that doesn't include the U.S. The code words for this rival version are "Western Pacific," and think tanks and leaders in Asia are still sorting out what this means. Sometimes it includes Australia, always Japan, the "four tigers," Southeast Asia, and China. But not the U.S. or Canada.

One such Western Pacific proposal came from Australian Prime Minister Robert L. Hawke, who is proposing an

Tokyo must overcome the painful memories Asians have of exploitation and occupation

Asia-Pacific body resembling the Paris-based Organization for Economic Cooperation & Development. Thailand has proposed a consultative body consisting of Japan, China, Korea, Taiwan, Hong Kong, and the six members of the Association of South East Asian Nations (ASEAN) to serve as a counterbalance to North America and Europe. Japan's ruling Liberal Democratic Party also has a study group on Asian affairs that solicits representatives from Asia but not North America. Says Toshio Watanabe, development economist at the Tokyo Institute of Technology: "The talk is still vague and ill-defined, but Japan's new nationalism is real, and it is intimately linked with Asianism."

As a leader, Japan makes a show of being reluctant. But surfaces are notoriously deceptive in Asia. Japan knows it cannot take the initiative without incensing other Asians, who remember Japan's colonial atrocities. "History confronts Japan full-face when it tries to emerge in the Pacific region with any initiative," says Mark Borthwick, U.S. director of the 15-nation Pacific Economic Cooperation Conference.

Japan, however, is beginning to show a subtle but powerful leadership. Its officials are speaking out internationally on behalf of other Asians. They are developing partnerships with the U.S. and Australia to manage the problems of Asia. Tokyo's Foreign Affairs Ministry, for example, is affiliated with the Carnegie Council's \$750,000, three-year Philippines project. The ministry also takes part in the Pacific Economic Cooperation Conference.

'Japanies.' A new pun has even entered the regional vernacular to describe Japan's deepening relations with Asia's newly industrializing economies (NIEs). Some products made in these countries have been nicknamed "Japanies." The reason is that Japanese companies have transferred so much of their production to Asia. Aiwa Co., the consumer electronics company, now makes half its products in Singapore. Minebea Co., the ball bearing and electronic components

company, has invested \$400 million in five plants in Thailand and plans an additional \$240 million worth. Toshiba is investing \$130 million in half a dozen projects in Thailand, making refrigerators, color televisions, electric motors, and fans—all mostly for export. Says Bank of Thailand's governor, Kamchorn Sathirakul: "A few years back we had no hope to export back to Japan. Now more and more products made in Thailand are exported to Japan."

Japanese companies that invest elsewhere in Asia and ship parts and products throughout the region are driving

to the U.S., Washington forces countries to look elsewhere. U.S. pressure—whether on tariffs, exchange rates, or protection of intellectual property rights—actually helps boost Japan's prestige in the region, allowing it to act as Asia's benefactor. "If America pushes too recklessly, you risk crushing these economies," says Masao Toyoda, director for international policy at Japan's Ministry of International Trade & Industry (MITI).

TOUGH NUT. Encouraging Japan to regional leader has other risks for

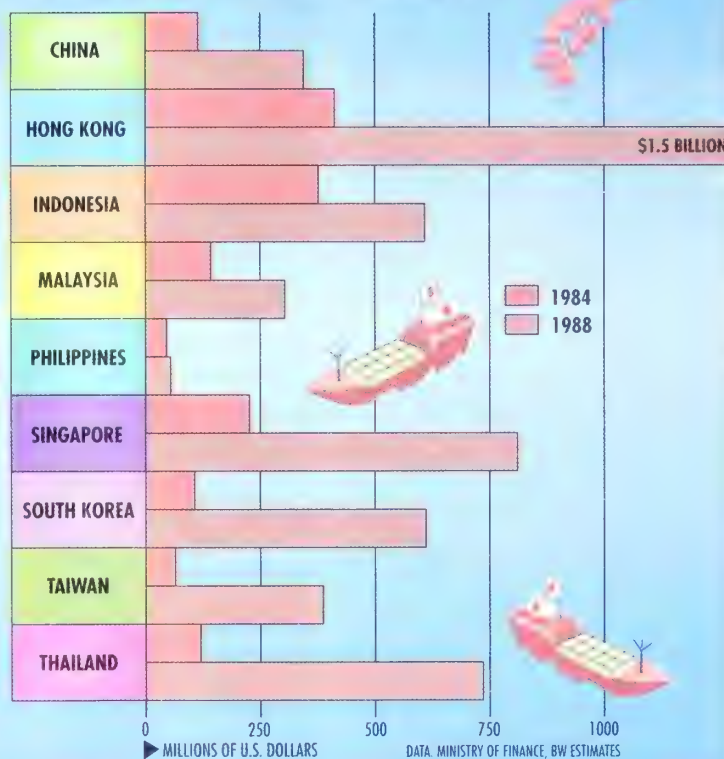
U.S. Japanese investment in Asia helps create new products aimed at the U.S. market. Increasing Japanese means there are always ways for its companies to win big projects and make sales. The Southeast Asian representative for Schlage Door Hardware International is the U.S. company is frozen out of contracts because Japanese construction companies working on Japanese-funded projects specify Japanese products as standard equipment. "You are before you start," he says.

Technology market also become tougher. Fujitsu Ltd. and NEC Corp. are sweeping up in Asia's digital communications markets. And the Japanese also started to bid Asian bids for supercomputers—the big number-crunchers represent one of America's last bastions of computer superiority. Because government

are the main customers, Japan can use its foreign aid as a lever. Overall, exports to East Asia, excluding Japan, increased by 77%, to \$47 billion, from 1986 to 1988. But the Americans are in deficit, and further progress will be hard, in part because of tough, entrenched competition from Japan.

In many areas, American companies are simply not rising to the challenge. In recent years, when Japanese department stores were eagerly rushing into Southeast Asia to take advantage of rising consumer demand, Americans stood on the sidelines. While Japanese, Korean, and Taiwanese are setting up new

JAPAN'S INVESTMENT IN ASIA IS GROWING



the surge in trade, including exports to Japan. Trade within Asia is growing at a 30% annual clip, and Phisit Pakkesem, deputy secretary general of Thailand's National Economic & Social Development Board, predicts it will surpass the region's \$250 billion in two-way trade with the U.S. by 1991. By 1995, he thinks, the U.S. market will be marginal. This process, adds Watanabe, "leads to natural market integration in Asia, even without a formal, institutional framework."

In some senses, the Americans are driving Asia into Tokyo's arms. By making it more difficult for Asians to export

ries in Bangkok and Penang, U.S. companies cut back in Asia the minute they get into trouble at home. Seagate Technology and Miniscribe Corp., for example, recently laid off their Asian workers by the hundreds.

CONTEST. Many U.S. companies are expanding their Asian presences, but these often are expansions of existing facilities. Last October, Texas Instruments Inc. announced plans to invest \$4 million to expand its semiconductor facility in Singapore, and American Telephone & Telegraph Co. is spending \$25 million to expand its telephone factory here. Others, such as Compaq, Wyse Technology, Motorola, General Electric, 3M Chemical, and Corning, are putting new investments in place. But the overall U.S. expansion is not as fast as it once was—and pales in comparison with the dramatic plunges many Japanese companies are taking. Says Peter L. Ravoir, vice-president of IBM's Asia/Pacific Group in Tokyo: "We [Americans] are all going to have to run very fast to stay here."

Staying in the Asian game, whether in terms of markets or broader geopolitical influence, shapes up as a challenge just as large as dealing with Soviet leader Mikhail S. Gorbachev or preventing Europe after 1992 from becoming Fortress Europe. "The future for us in Asia is not easy," says Robert B. Oxnham, president of the Asia Society based in New York. "What was an Asian world fraught with strategic and military questions in the early 1980s is going to be fraught with economic, investment, and protectionist questions in the 1990s."

American experts on Asia argue that the U.S., rather than panicking at Japan's expanding clout there, should look at this change as a stimulus. Because of disparities in the size and nature of their economies and their deep historical bonds, the Asians are at least a decade behind the Europeans in forming any kind of formal regional economic body. Korea and Taiwan also are emerging as major investors in the region, and the growing trade among non-Japanese Asian economies will help to dilute Tokyo's influence.

The new Asia Co-Prosperity takes on ominous coloring only if the Americans fail to maintain vital economic connections with the region. If the U.S. forces Asians to retreat into a protective cocoon, history could repeat itself. Asians argue, optimistically, that a rising tide of prosperity in the region will sweep all ships. Perhaps, but it is up to the Americans to make sure that they remain part of the fleet.

Dori Jones Yang in Bangkok and Neil R. Jones in Tokyo, with William J. Holstein in New York, Dirk Bennett in Taipei, Larxi Nammi in Seoul, and bureau reports

SOUTH KOREA



UNITED THEY SIT: A MONTHS'-LONG STRIKE HAS PARALYZED HYUNDAI'S SHIPYARD IN ULSAN

IT'S TIME FOR THE MAIN BOUT: ROH VS. LABOR

Violence and union demands are challenging the Korean government

Fighting among moderate and radical union members has paralyzed Hyundai Heavy Industries Co.'s sprawling shipyard in Ulsan for 3½ months. Violence has resulted in more than 300 injuries, and production losses have reached \$760 million. On Mar. 16, President Roh Tae Woo used force to break up a strike by 5,000 Seoul subway workers. Overall, 216 labor disputes broke out in 1989's first quarter, double the number in that period last year.

South Korea's annual labor push is on, and it promises to be the country's highest-stakes contest since it moved toward democracy. Korean business leaders say they cannot grant further sharp wage increases and remain competitive. They are offering only half as much as the unions are demanding, making more confrontation inevitable. "The worst is yet to come," admits Han Seung Soo, the Trade & Industry Minister.

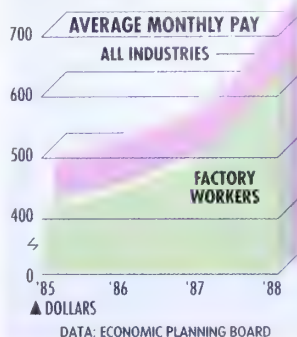
The labor offensive is also shaping up as a decisive political test for Roh. With radical students and political dissidents playing active roles, militant union leaders are openly challenging the authority of Roh's government.

"Our aim is to force antilabor and military dictator Roh Tae Woo out of office," says Tan Byung Ho, an official of the National Council of Trade Unions, a dissident-led coalition formed to coordinate labor activities. Roh's opponents hope to create enough disorder to force him to resign.

HANDS-OFF? The new, intensified conflict among unions, business, and government is likely to peak in May, when the unions plan a nationwide strike. Unlike last year, when the government adopted a hands-off approach, Roh has warned he will deal more strongly with labor violence and illegal activities. On Mar. 24, Roh vetoed a bill providing a shorter workweek and allowing teachers and low-level government employees to form unions. He has indefinitely postponed a promised referendum on his rule that was widely expected in April and has issued M-16s to police—with orders to shoot firebomb-throwing attackers.

But Roh's tougher stance still does not satisfy his critics on the right. The military is particularly unhappy about Roh's failure to check the rapid increase in leftist influence. In

BIGGER RAISES FOR KOREAN WORKERS



late March, Roh retired the three-star general who was superintendent of the Korea Military Academy, the country's equivalent of West Point, for refusing to salute the President during a commencement ceremony. Some Korea-watchers are worried that groups of former military officers will start taking action against dissidents, much as some companies have organized *kusade*, or save-the-company groups, to attack disruptive workers.

'SERIOUS SETBACK.' Aside from the political hazards, another bitter round of labor confrontation could be devastating economically. Korea has been able to absorb wage increases averaging 20% over the past two years, but now government and business leaders are warning that further big increases could cripple Korea's economic miracle. The government, already concerned about double-digit inflation and slower growth in exports, believes prolonged labor disputes and sharp wage increases could slow the economy to about 6% growth this year, compared with 12% in each of the past three years. "Without an early solution, the Korean economy might face a serious setback," says Deputy Prime Minister Cho Soon, who is Korea's chief economic policymaker.

That argument is not going to be persuasive, however, among the rank and file. Even moderate labor leaders argue that Korean workers are being denied their fair share of Korea's economic success. Factory workers in particular have lagged behind other sectors (chart, page 45). Thus the moderate Federation of Korean Trade Unions is demanding an average wage increase of 26.8% this year, against the 12.9% being offered by employers. "Laborers should not be sacrificed to keep Korea competitive," says Hong Sams Hee, secretary general of the federation. "Competitiveness should be maintained not by keeping wages low but by enhancing efficiency in production and management."

Roh's room to maneuver on the labor front is severely constrained by the unending controversy over the abuses of his predecessor, Chun Doo Hwan, who has been exiled to a Buddhist monastery. Allegations about Chun's corruption and brutality have strengthened Kim Dae Jung, the leader of the largest opposition party, who is warning Roh about the use of too much force against unions. If Roh were to crack down too hard on union activity, it would hand a major new issue to opponents who already have the President on the defensive. Faced with widening chasms among his countrymen, Roh's tightrope act is growing ever more perilous.

By Larri Nakarmi in Seoul

FRANCE

A MARRIAGE OF GIANTS TO DEFEND FRENCH FINANCE

Jean Peyrelevalde is linking a state-run bank and an insurance firm



PEYRELEVALDE: "THE BEST WAY TO FEND OFF COMPETITION IS TO BECOME STRONGER"

Jean Peyrelevalde is emerging as one of Europe's most powerful—and protectionist-minded—financiers. And it's not just because he's a staunch Socialist whose friends include Finance Minister Pierre Bérégovoy and Industry Minister Roger Fauroux. An engineer by training, the 49-year-old Peyrelevalde has proved a quick study. A political appointee running *Compagnie Financière de Suez* after it was nationalized in 1982, Peyrelevalde later became head of privately owned *Banque Stern*. Now he's in insurance as chairman of the huge, state-run *Union des Assurances de Paris* (UAP). Combining his banking and insurance knowhow, he wants to build a French-style financial supermarket able to keep foreign competitors at bay.

Peyrelevalde's plans are similar to those of other financial conglomerates elsewhere in Europe. Free from such restrictions as America's Glass-Steagall Act, many European banks long have offered consumers one-stop shopping for deposits, loans, and securities. But the latest wrinkle is insurance. In West Germany, *Dresdner Bank* and insurer *Allianz* have joined forces. Britain's *Abbey Life Group* and *Lloyds Bank* have done likewise. The French version will join UAP with state-owned *Banque Nationale de Paris* (BNP), Europe's largest com-

mercial bank, with \$155 billion in assets.

These new behemoths hope to protect their home turfs when a single European Community-wide money market is created in 1992. Says Peyrelevalde: "The best way to fend off competition is to become stronger in one's own home market." If size is the best protection, UAP and BNP will be in good shape. They have combined assets of \$187 billion, annual revenues of \$12.6 billion, and employ 86,000. But although the two companies will acquire up to a 10% interest in each other for about \$380 million, they will remain separate entities.

Economic nationalism is also guiding the UAP-BNP deal. Peyrelevalde holds that French companies must be protected from foreign raiders. He expects that by pooling resources, UAP and BNP will enable the government to acquire blocks of shares in undercapitalized French companies. Says a Peyrelevalde aide: "He wants to create an institution that can act powerfully."

PROBLEM-SOLVER. Peyrelevalde has a penchant for lecturing on the survival of French industry to the point where he has antagonized Frenchmen and outsiders alike. However, he is a proven problem-solver. Among his accomplishments: Lining up French financing for the Eurotunnel under the English Channel and helping persuade Walt Disney Co. to build Euro Disneyland outside Paris.

He already is taking a no-nonsense approach to capitalize on UAP's and BNP's strengths. In September, UAP's insurance agents will begin offering BNP car loans, home mortgages, and revolving credit lines. And BNP will offer UAP auto insurance and home policies in some offices. Later on, the two companies plan to sell a full line of each other's products to their combined roster of 10 million customers.

With an array of "Made in France" products and low prices based on economies of scale, Peyrelevalde hopes French consumers will never be lured away by the competition. The real test will come when British and German banks and insurers attempt to flood French market in 1992. Bankers from outside France give the edge to the home team, but promises to be a bruising showdown.

By Blanca Riener, with Frank Comes, in Paris

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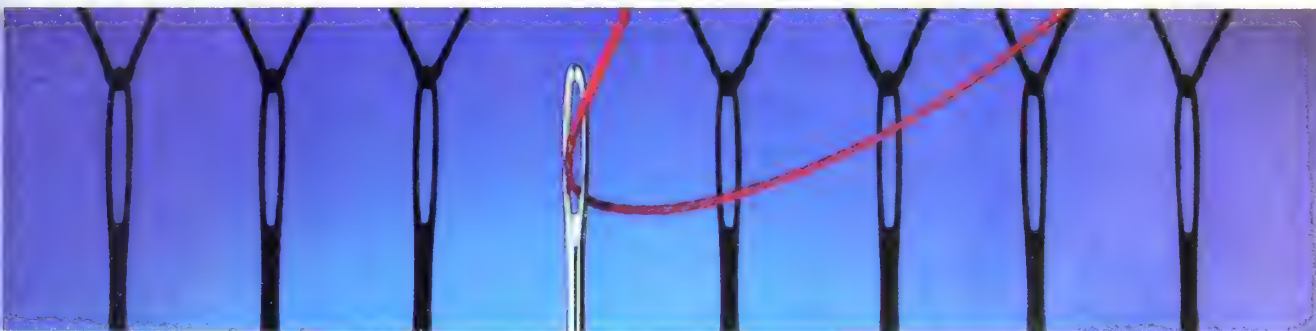
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TALK TO THE PLO? MORE ISRAELIS ARE THINKING ABOUT IT

In The Hague, former Israeli Foreign Minister Abba Eban talked with officials of the Palestine Liberation Organization last January. In East Jerusalem, other senior Labor Party members met in recent weeks with PLO representatives in the home of Faisal Hussein, a Palestinian leader released not long ago from an Israeli jail. By contrast, Prime Minister Yitzhak Shamir, the leader of Israel's conservative Likud bloc, almost daily warns that he will never negotiate with the PLO. But the signs are clear. The rock-hard consensus that Israelis maintained for years against dealing with the PLO is crumbling.

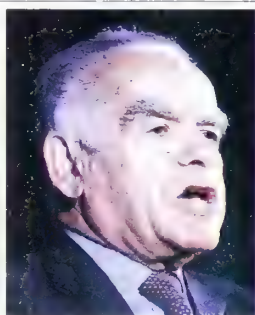
So also may be the taboo that limited debate on the future status of the West Bank and Gaza. Up to now, Israel's leaders could be counted on to reject any suggestion that a separate Palestinian state could be allowed in these territories. But just last month reports surfaced that Labor Party leader Shimon Peres, who serves as Finance Minister in the Labor-Likud government, was drawing up a new peace plan which included negotiations that could lead to a demilitarized Palestinian state. Although Peres denied the reports, Labor leaders say growing opinion within the party supports such an approach. Peres did say that "we shall not be able to achieve peace without a historic compromise involving a rearrangement of territories and boundaries," and he added that Israel should negotiate with representatives chosen by Palestinians in the occupied lands. Few Israelis doubt that any designated negotiators would have to have PLO approval.

ONGOING CLASHES. These deepening divisions within Israel on how to make peace are likely to surface more clearly when Shamir arrives in Washington on Apr. 4 bearing his own proposals to end the conflict. Unlike previous American leaders, President Bush is not offering any U.S. blueprint, such as Carter's 1978 Camp David formula or Reagan's peace plan of 1982. Instead, Bush is relying on the Palestinians' 16-month *intifada*, or uprising, to build pressure among Israelis and

Palestinians to find a formula for a settlement. So far, the most pressure has been on Israel, which is losing political support in the U.S. because of the Israeli army's harsh tactics against Palestinian protesters.

What Shamir has in mind appears to be an updated Camp David plan for Palestinian autonomy, including municipal elections, as a step toward eventual talks on a final settlement. That could be a formula for a continued impasse, however, because the PLO spurns elections under Israeli domination and has proclaimed an independent Palestinian state in the West Bank and Gaza. Shamir, for his part, rejects a swap of occupied land for peace. With Bush keeping the U.S. relatively aloof, Shamir seems likely to return to Jerusalem without a U.S. endorsement for his plan. That will add fuel to the debate in Israel over how to deal with the Palestinians.

Senior Labor Party officials, such as Science Minister Ezer Weizmann and Deputy Finance Minister Yossi Beilin, a close aide to Peres, want to negotiate directly with the PLO. So do all political parties to the left of Labor. Reagan gave U.S. support to this approach when he allowed the American ambassador in Tunisia to open talks with PLO officials, and Israeli institutions also



SHAMIR: NO LAND SWAP

suggest that Israel sooner or later will bargain with Arafat. A recently leaked Israeli military intelligence report and a Tel Aviv University study concluded that Israel would have to deal with the PLO for lack of any alternative.

Arab states are trying to speed this process. Jordan and Egypt, with backing from Saudi Arabia's King Fahd, are working closely with the PLO. Soon after Shamir's visit to Washington, Egypt's President Hosni Mubarak and Jordan King Hussein will arrive there to urge a settlement. In the PLO's bid for a legitimate role in the peace process, Egyptian support is important because it broke the Arab taboo against making peace with Israel. Eventually, Israel seems destined to follow Egypt's example by making peace with the PLO.

By Neal Sandler in Jerusalem and Bill Javetski in Washington

GLOBAL WRAPUP

POLAND

Polish society "is undergoing a change of skin, and any snake can tell you how painful this can be." Jerzy Urban, the Polish government's spokesman, offered that metaphor to explain the current protracted negotiations in Warsaw when he arrived in the U.S. in late March to "help Americans understand Polish reforms." Solidarity, the independent union, and the government expect to sign a pact in early April aimed at opening the Marxist political system to legal opposition and the economy to private enterprise.

In talks with U.S. officials, Urban hopes to win Washington's backing for

an International Monetary Fund loan to smooth Poland's transition and ease its \$40 billion debt. If the Warsaw talks are successful, Urban says, Solidarity and the Polish government will issue a joint statement asking for such help from the West. In fact, the need to gain credibility by winning Solidarity's support for steps to shore up the tottering economy is the government's main motive for negotiating reforms.

TURKEY

Stunning losses by his Motherland Party in Mar. 26 local elections are expected to force Prime Minister Turgut Ozal, an advocate of freer markets, to call early elections. Defections

from his party in parliament could send him to the polls as early as next spring, although his current term runs to 1992.

The electoral rebuff, reflecting a backlash against Turkey's 75% inflation, dropped Motherland behind the conservative True Path Party and the Social Democratic Party in total votes. Even so, the results do not appear to signal a major political turn. True Path differs little from Motherland in basic outlook, and the Social Democrats, although they oppose privatizing some state-run companies, share Ozal's commitments to freer markets, the NATO alliance, and eventual Turkish membership in the European Community.

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Commentary/by Paul Magnusson

A NATIONAL LOTTERY IS NOT SUCH A LONG SHOT

Imagine a tax nobody is required to pay—yet it raises billions of dollars. Imagine that people gladly stand in line to pay it—but no one considers it a burden. A fantasy? Not at all. It's a government lottery.

That's not a tax, you say, it's just gambling. Well, it is gambling, but to many economists it is also an excise on a commodity—a lottery ticket that happens to be supplied by a government monopoly that sets the price.

This year, 28 states and the District of Columbia are running lotteries, which have been the fastest-growing source of state revenues in the 1980s (chart). The strapped federal government may soon want to follow suit.

Republicans and Democrats are deadlocked over how to cut the budget deficit, and no one wants to be first to take up the cudgel. Alone among major revenue raisers, however, lotteries pass the White House "duck" test.

A lottery doesn't look, walk, or sound like a tax. Instead, most people regard lotteries as harmless fun. For a buck, you can fund the trip home from work without thinking on how you would run through a million dollars.

Enough people are indulging in the musings to give the states lottery impressive returns. In big states such as California and Florida, lotteries have been grossing more than \$100 a year per adult. Nationally, that would translate into \$19 billion.

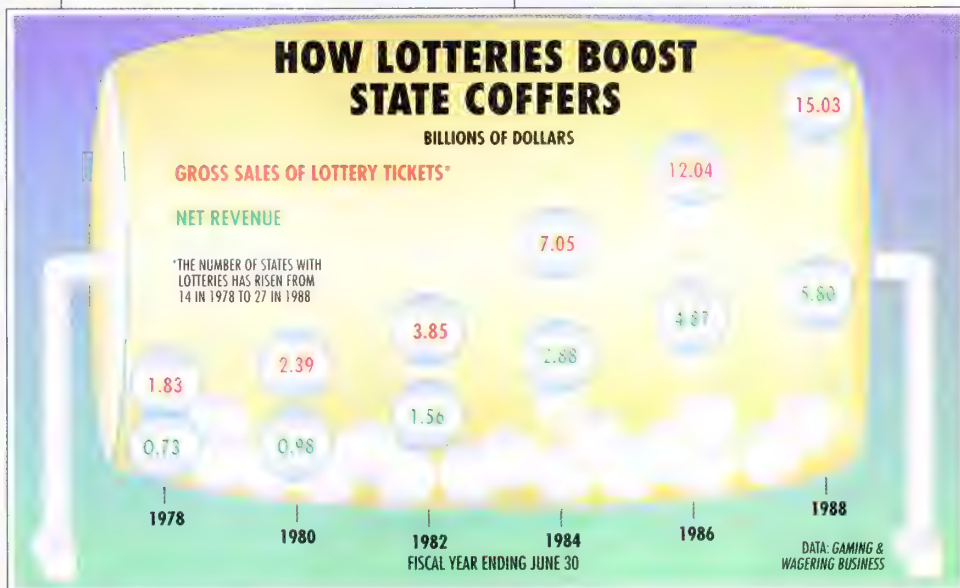
10-FORM BETS. State lotteries have been spending about half their income on prizes, spending 15% on administration, and pocketing the remaining 34%. Economies of scale and new computer technology should enable the federal government to net even more. Experts say administrative costs could be far lower, with bets placed by mail at computer terminals in post offices, instead of at local vendors. Taxpayers could check off on their 1040 forms the annual amount they want to contribute. That would attract "people who might be embarrassed to step up and make a bet publicly," says Charles Kefauver, Duke University economist. If the federal government could keep 40% of the receipts—\$7.6 billion

of \$19 billion, say—that approximates a tax of \$5 to \$7.50 per barrel on imported petroleum. Or a gasoline tax hike of 10 cents a gallon. Or a 5% corporate income tax surcharge.

Any national lottery has plenty of opposition to overcome: The states worry about competition from the feds, intellectuals voice disdain for such simple fun, and moralists howl about gambling's corrosive impact on the poor. Author George Orwell saw a future in

Technology. That may be because purchasing a lottery ticket can't match the thrill of the track or the adrenaline rush of beating the point spread.

FULFILLED LIVES. Interestingly, Kaplan's research over 20 years destroys another myth: that million-dollar jackpot winners' lives are shattered. Instead, research shows that they benefit from the increased financial security, have fewer divorces than other people, don't take up serious gambling, and



which a crooked national lottery kept the "proles" preoccupied and docile.

But the U.S. is fast moving toward a backdoor national lottery anyway. States are banding together to offer ever larger prizes, such as the seven-state Lotto America. And some experts believe that one or more state-sponsored lotteries operating nationwide may be next, with proceeds going to participating states. Many of those states, which have been running budget surpluses during the 1980s, could afford to lose their monopoly.

True, a lottery is regressive: Buying a ticket eats up a bigger slice of a poor man's income than of a rich man's. But there is no hard evidence that the games are wreaking havoc. "You don't find too many people abusing lotteries—not like with the more insidious gambling: sports betting, casinos, and race tracks," says H. Roy Kaplan, a sociologist at the Florida Institute of

usually quit their jobs only for a good reason, such as going back to school to train for a new career. "All us losers can't seem to bear the idea that the winners are happy," he says.

Moralistic arguments are tougher to overcome. Some churches, however, have done so, earmarking bingo proceeds for high-minded causes. In appealing to altruism, a national lottery could shine, too. Worried about the environment? Play the Environmental Protection Agency's Green Lottery.

Still, there is something unseemly about the world's greatest economic power stooping to such gimmickry to balance its books. Hemingway used to complain that Third World countries were distinguished by tardy trains, bad water, and lotteries. But with both Democrats and Republicans in their annual budget deadlock, why dwell on such fine points? Let the games begin.



MASTERS OF INNOVATION

HOW 3M KEEPS ITS NEW PRODUCTS COMING

It was 1922. Minnesota Mining & Manufacturing inventor Francis G. Okie was dreaming up ways to boost sales of sandpaper, then the company's premiere product, when a novel thought struck him. Why not sell sandpaper to men as a replacement for razor blades? Why would they risk the nicks of a sharp instrument when they could rub their cheeks smooth instead?

The idea never caught on, of course. The surprise is that Okie, who continued to sand his own face, could champion such a patently wacky scheme and keep his job. But unlike most companies then—or now—3M Co. demonstrated a wide tolerance for new ideas, believing that unfettered creative thinking would pay off in the end. Indeed, Okie's hits made up for his misses: He developed a waterproof sandpaper that became a staple of the auto industry because it produced a better exterior finish and created less dust than conventional papers. It was 3M's first blockbuster.

Through the decades, 3M has managed to keep its creative spirit alive. The result is a company that spins out new products faster and better than just about anyone. It boasts an impressive catalog of more than 60,000 products, from Post-it notes to heart-lung machines. What's more, 32% of 3M's \$10.6 billion in 1988 sales came from products introduced within the past five years. Antistatic videotape, translucent dental braces, synthetic ligaments for damaged knees, and heavy-duty reflective sheeting for construction-site signs are just a few of the highly profitable new products that contributed to record earnings of \$1.15 billion in 1988.

At a time when many big U.S. corporations are trying to untangle themselves from bureaucracy, 3M stands apart as a smooth-running innovation machine. Along with a handful of other

companies that might be called the Innovation Elite—Merck, Hewlett-Packard, and Rubbermaid among them (page 62)—3M is celebrated year after year in the rankings of most-respected companies. Business schools across the country make 3M a case study in new-product development, and management gurus trumpet 3M's methods. Peter Drucker's *Innovation and Entrepreneurship* is peppered with 3M tales. A star of the bestseller *In Search of Excellence*, 3M remains a favorite of co-author Thomas J. Peters. "It is far more entrepreneurial than any \$10 billion company I've come across," he says, "and probably more entrepreneurial than a majority of those one-tenth its size."

The publicity has attracted representatives of dozens of companies from around the world to tour 3M headquarters near St. Paul, Minn., in search of ideas and inspiration. While such companies as Monsanto Co. and United Technologies Corp. have adopted some of 3M's methods, it's hard to emulate a culture that has been percolating since the turn of the century.

LOSE SOME. So how does 3M do it? One way is to encourage inventive zealots like Francis Okie. The business of innovation can be a numbers game—the more tries, the more likely there will be hits. The scarcity of corporate rules at 3M leaves room for plenty of experimentation—and failure (page 62). Okie's failure is as legendary among 3Mers as his blockbuster. Salaries and promotions are tied to the successful shepherding of new products from inception to commercialization. One big carrot: The fanatical 3Mer who champions a new product out the door then gets the chance to manage it as if it were his or her own business.

Since the bias is toward creating new



PAYOFF ►
Tony Flannery developed a filter for metalworking shops—a mere \$1 million market. R&D funds led him to markets 20 times bigger

TAKING AN IDEA AND RUNNING WITH IT



▲ **HIGH NOTES**
Post-its, demonstrated by 3M engineers Art Fry, left, and Spencer Silver, began life as a way to keep bookmarks from slipping out

◀ **R&D FIRST**
Jake Jacobson has cracked a tough nut by cutting costs without hurting R&D efforts



▲ **SHINER**
Sanford Cobb won an in-house grant to develop the use of plastic film in lighting—a profitable breakthrough

products, anything that gets in the way, whether it's turf fights, overplanning, or the "not-invented-here" syndrome, is quickly stamped out. Divisions are kept small, on average about \$200 million in sales, and they are expected to share knowledge and manpower. In fact, informal information-sharing sessions spring up willy-nilly at 3M—in the scores of laboratories and small meeting rooms or in the hallways. And it's not unusual for customers to be involved in these brainstorming klatches.

PEER REVIEW. That's not to say that corporate restraint is nonexistent. 3Mers tend to be self-policing. Sure, there are financial measures that a new-product team must meet to proceed to different stages of development, but the real control lies in constant peer review and feedback.

The cultural rules work—and go a long way toward explaining why an old-line manufacturing company, whose base products are sandpaper and tape, has become a master at innovation. And a highly profitable one at that. Earnings spurred 25% in 1988 from a year earlier. It wasn't always so. The company hit a rocky stretch in the early 1980s. But stepped-up research spending and some skillful cost-cutting by Chairman and Chief Executive Allen F. Jacobson have revived all of 3M's critical financial ratios.

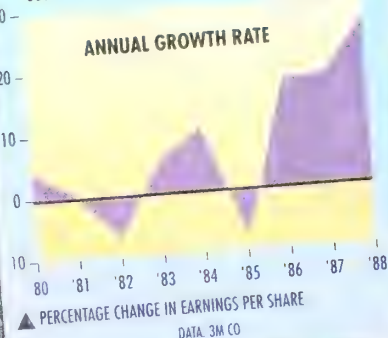
A 3M lifer and Scotch-tape veteran, Jake Jacobson took over the top job in 1985 and laid out his J-35 program. That's J as in Jake, and 35 as in 35% cuts in labor and manufacturing costs—to be accomplished by 1990. 3M is well on its way to reaching those goals, and the push has already improved the bottom line. Last year return on capital climbed almost three points, to 27.6%, and return on equity had a similar rise, to 21.6%. Jacobson has clamped down on costs without harming his company's ability to churn out new products one whit.

MOTLEY CREW. 3M was founded not by scientists or inventors but by a doctor, a lawyer, two railroad executives, and a meat-market manager. At the turn of the century the five Minnesotans bought a plot of heavily forested land on the frigid shores of Lake Superior, northeast of Duluth. They planned to mine corundum, an abrasive used by sandpa-

3M'S PUSH FOR PRODUCTS AND PROFIT MORE RESEARCH SPENDING...



...HELPS THE BOTTOM LINE



per manufacturers to make the paper scratchy. The five entrepreneurs drummed up new investors, bought machinery, hired workers, and started mining. Only then did they discover that their corundum, alas, wasn't corundum at all but a worthless mineral that the sandpaper industry wanted no part of.

The company tried selling its own sandpaper, using corundum shipped in from the East, but got battered by the competition. How perfect: The company that tolerates failure was founded on a colossal one. 3M was forced to innovate or die. Most of the original investors got swept out of the picture, and the remaining 3Mers set about inventing. First, the company introduced a popular abrasive cloth for metal finishing. Then Okie struck gold with his Wetordry sandpaper. They drew inspiration from William L. McKnight, who is revered to this day as the spiritual father of the company. He started out as an assistant bookkeeper and worked his way up through sales. His approach, unusual for its day, has stuck with the company. Rather than make his pitch to a company's purchasing agent, McKnight talked his way onto the factory floor to demonstrate his products to the workers who used them. After he became chairman and chief executive, he penned a manifesto that said, in part: "If management is intolerant and destructively critical when mistakes are made, I think it kills initiative."

LOYAL LIFERS. That kind of thinking breeds loyalty and management stability. The company rarely hires from the outside, and never at the senior level. Jacobson, 62, a chemical engineer, started out in the tape lab in 1947. And all his lieutenants are lifers, too. The turnover rate among managers and other professionals averages less than 4%. "It's just not possible to really understand this company until you've been around for a long while," says Jerry E. Robertson, head of the Life Sciences Sector.

Don't let 3M's dull exterior fool you. The St. Paul campus, home of company headquarters and most of the research labs, is an expanse of brick buildings with a high-rise glass tower that could have been designed by a kid with an Erector set. But inside is an army of engineers and technical experts and platoons of marketers just raring to innovate.

Here's how it typically works: A 3Mer comes up with

INSPIRATION FROM THE PLANT FLOOR

When I worked as a tape at 3M, we called them T. They were the button members of the 3M Co. quality team who would occasionally venture the grimy factory floor.

"They were the bad guys," says Vernon, who runs a slitting machine that converts huge rolls of tape into the ones you buy in the store. "They tell you rather than listen to you, saying they even spoke to you in the place." I worked alongside Vernon years ago, running my own machine, making masking tape so I could come to college tuition. 3M paid me well above the standards of the day, treated me well. But despite all the talk I had heard of 3M and innovation, nobody ever asked for ideas on how to do my job better. At least of all the guys from quality control.

That was 1973. Today, 3M's tape business is under assault from Japanese and European manufacturers. Over the years while researchers at headquarters

an idea for a new product. He or she forms an action team by recruiting full-time members from technical areas: manufacturing, marketing, sales, and maybe finance. The team designs the product and figures out how to produce and market it. Then it develops new uses and line extensions. All members of the team are promoted and get raises as the project goes from hurdle to hurdle. When sales grow to \$5 million, for instance, the product's originator becomes a project manager, at \$20 million to \$30 million, a department manager, and in the \$75 million range, a division manager. There's a separate track for scientists who don't want to manage.

MANY PATHS. As a result, 3M is big but acts small. There are 42 divisions, so ladders to the top are all over the place. Jacobson reached the pinnacle by cleaning up old-line operations, while his predecessor, Lewis W. Lehr, invented

ved out new products, innova-
's factories lagged. By the ear-
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asn't up to snuff. Productivity
top priority for Chairman and
F. Jacobson, who worked his
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aims to cut labor and manufac-
ts by 35% each.

The edict forced major change
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iant roll about the size of an
sk. These "jumbos" are then
slitting machines. Until recently,
at the plant—masking tape, in-
apes, closure tape for diapers—
ed in one area and transported
g to the other end of the fac-
coating and slitting functions
ate supervisors, and they didn't
communicate well. Production
en't coordinated, and hundreds
s were stockpiled throughout

litters are placed near the
nd management duties are de-



SLITTING TAPE: NOW THE OPERATOR IS EXPECTED TO SPOT QUALITY PROBLEMS

terminated by product line, not function—that is, a supervisor will be in charge of masking tape, not just coating or slitting. The new setup puts a lot more responsibility on the shoulders of individual workers. A slitting operator is expected to identify quality problems immediately so he or she can have the coater stopped after only two or three bad jumbos are produced, rather than the dozens botched in the past. As a result, inventory has

been trimmed dramatically. And manu-
facturing time has improved by two-
thirds.

The workers with whom I talked ap-
preciate the new responsibilities. I had
hated feeling like an automaton when I
worked in the 3M plant, but it's an en-
tirely different story these days for my
former colleagues. They don't miss The
Ties at all.

By Russell Mitchell in Bedford Park, Ill.

urgical tape and then rode the compa-
burgeoning health care business all
way to the chairman's post.

o what are the corporate guidelines?
rime one is the 25% rule, which re-
ves that a quarter of a division's sales
e from products introduced within
past five years. Meeting the 25% test
crucial yardstick at bonus time, so
agers take it seriously. When Rob-
J. Herschok took over the occupa-
tional health division in 1982, it
was utterly de-

pendent on an aging product category,
disposable face masks. By 1985 his new-
product percentage had deteriorated to a
mere 12%.

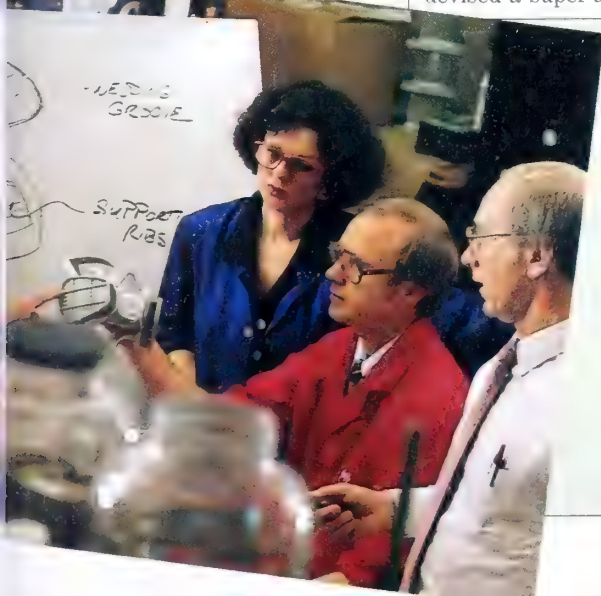
That set off alarms. He and his crew
had to come up with plenty of new prod-
ucts—and they had to do it in 18 to 24
months, half the normal time. Using
technology similar to the division's face-
mask filters, Herschok's action teams
created a bevy of products. One team
came up with a sheet that drinks up the
grease from microwaved bacon. Another
devised a super-absorbent packing mate-

rial that was widely welcomed by han-
dlers of blood samples. The idea came
from a team member who had read a
newspaper article about postal workers
who were panicked by the AIDS epidemic.
The division's new-product sales are
back above 25%.

Then there's the 15% rule. That one
allows virtually anyone at the company
to spend up to 15% of the workweek on
anything he or she wants to, as long as
it's product-related. The practice is called
"bootlegging," and its most famous in-
novation is the ubiquitous yellow Post-it
note. Arthur L. Fry's division was busy
with other projects, so he invoked the
15% rule to create the adhesive for Post-
its. The idea came out of Fry's desire to
find a way to keep the bookmark from
falling out of his hymn book. Post-its are
now a major 3M consumer business,
with revenues estimated at as much as
\$300 million.

CULTURAL HABITS. A new-product ven-
ture isn't necessarily limited by a particu-
lar market's size, either. Take Scotch
tape. It was invented in 1929 for an in-
dustrial customer who used it to seal
insulation in an airtight shipping pack-
age. Who could have known that it
would grow into an estimated \$750 mil-
lion business someday?

Another recent example: The market



LIGHTS, ACTION
3M light pipes top
off Philadelphia's
One Liberty Plaza,
far left. Above,
employees from
various disciplines
discuss the design
of a respirator

CORPORATE INNOVATORS: HOW THEY DO IT

3M RELIES ON A FEW SIMPLE RULES...

Keep divisions small. Division managers must know each staffer's first name. When a division gets too big, perhaps reaching \$250 to \$300 million in sales, it is split up

Tolerate failure. By encouraging plenty of experimentation and risk-taking, there are more chances for a new-product hit. The goal: Divisions must derive 25% of sales from products introduced in the past five years. The target may be boosted to 30%

Motivate the champions. When a 3Mer comes up with a product idea, he or she recruits an action team to develop it. Salaries and promotions are tied to the product's progress. The champion has a chance to someday run his or her own product group or division

Stay close to the customer. Researchers, marketers, and managers visit with customers and routinely invite them to help brainstorm product ideas

Share the wealth. Technology, wherever it's developed, belongs to everyone

Don't kill a project. If an idea can't find a home in one of 3M's divisions, a staffer can devote 15% of his or her time to prove it is workable. For those who need seed money, as many as 90 Genesis grants of \$50,000 are awarded each year

... WHILE OTHER COMPANIES HAVE THEIR OWN APPROACHES

RUBBERMAID 30% of sales must come from products developed in the past five years. Looks for fresh design ideas anywhere; now trying to apply the Ford Taurus-style soft look to garbage cans. A recent success: stackable plastic outdoor chairs

HEWLETT-PACKARD Researchers urged to spend 10% of time on own pet projects; 24-hour access to labs and equipment; keeps divisions small to rally the kind of spirit that produces big winners such as its LaserJet laser printer

DOW CORNING Forms research partnerships with its customers to develop new products such as reformulations of Armor-All car polishes and Helene Curtis hair sprays

MERCK Gives researchers time and resources to pursue high-risk, high-payoff products. After a major scientific journal said work on anticholesterol agents like Mevacor would likely be fruitless, Merck kept at it. The drug is a potential blockbuster

GENERAL ELECTRIC Jointly develops products with customers. Its plastics unit created with BMW the first body panels made with thermoplastics for the carmaker's Z1 two-seater

JOHNSON & JOHNSON The freedom to fail is a built-in cultural prerogative. Lots of autonomous operating units spur innovations such as its Acuvue disposable contact lenses

BLACK & DECKER Turnaround built partly on new-product push. Advisory councils get ideas from customers. Some new hot sellers: the Cordless Screwdriver and Thunder Volt, a cordless powertool that packs enough punch for heavy-duty construction work

DATA COMPANY REPORTS

for 3M chemist Tony F. Flannery's product, a filter used to clean lubricants in metalworking shops, was a mere million. But Flannery got the go-ahead to dabble with it anyway. He hooked up with a customer, PPG Industries Inc., which sells paint-primer systems to auto makers. The filters they were using to strain out impurities weren't doing the job. Flannery made prototypes of filters using a fibrous 3M material. They not only turned out to be bang-up primary filters, but the new bags are also being used to filter beer, water, edible oil, machine oil, and paint. Flannery figures that the filters could become a \$20 million business in a few years.

Getting close to the customer is just a goal at 3M—it's an ingrained cultural trait. Back in the 1920s, 3M inventor Richard G. Drew noticed that painters on automobile assembly lines had trouble keeping borders straight on two-tone cars popular at the time. He went back to the lab and invented masking tape.

IN-HOUSE GRANTS. Even with 3M's emphasis on innovation, new ideas don't always get through the cracks. In 1983 some employees complained that worthwhile projects were still going unnoticed despite the 15% rule. Guaranteed free time doesn't guarantee that there will be money to build a prototype. So the company created Genesis grants, which give researchers up to \$50,000 to carry their projects past the idea stage. A panel of technical experts and scientists awards as many as 90 grants each year.

One recipient was Sanford Cobb, an optics specialist at 3M. In 1983 a bug went on in his head at a scientific conference when he ran across something called light pipe technology. Plastic inlaid with nearly microscopic prisms, it can reflect light for long distances with little loss of energy.

Cobb knew the heavy acrylic used in the original invention was impractical because it would be difficult to mold, but he figured he could use 3M technology to make a light pipe out of a flexible plastic film. Because 3M isn't in the lighting business, though, Cobb couldn't find a division manager willing to foot the prototype money. So he applied for a Genesis grant. He got it, and made the idea work.

CITY LIGHTS. 3M licensed the technology from the inventor, and now its light pipes are used in products offered by several divisions. One use is in large highway signs. The new ones feature two 400-watt bulbs, replacing 60 to 70 fluorescent tubes. Manufacturers of explosives use light pipes to illuminate their most volatile areas. At the top of One Liberty Plaza, the new



SE START
spective stockholders
1903 inspection tour of 3M's
d. The corundum, alas, proved to be no such thing

tower dominating Philadelphia's
 ie, is decorated with a light-piping
 n. Cobb's development is part of a
 new technology program at 3M,
 potential annual revenues amount-
) hundreds of millions of dollars.

a surprise, given 3M's strong pre-
 ion toward divisional autonomy,
 its technology gets spread around.
 M is a company of backscratchers,
 to help fellow employees in the
 ledge that they'll get help when
 need it in return. For example,
 the nonwoven-fiber experts got to-
 r with the lab folks at abrasives,
 result was Scotch-Brite scrubbing
 ges. A Technology Council made up
 researchers from the various divisions
 arly gets together to exchange
 nation.

e result of all this interconnection is
 ganic system in which the whole
 is greater than the sum of its
 . It's no coincidence that 3M is nev-
 entioned as a possible breakup can-
 e. Bust it apart, sever the intercon-
 ns, and 3M's energy would likely
 Even if a raider decided to leave it
 , an unfamiliar hand at the helm
 t send the company off course. The
 oility of a raid on 3M was taken a
 ore seriously in the early 1980s,

financial performance slipped as
 result of a strong dollar and skimp-
 n R&D in the 1970s.

obson's cost-cutting has done won-
 for 3M. But his next challenge is
 idable. The company's fortunes

tend to track the domestic economy, so
 with a slowdown on the horizon, he must
 now find ways to spur growth. For one,
 he wants to expand internationally,
 boosting overseas sales from 42% of rev-
 enues to 50% by 1992. It may be slow
 going, however. Just as Jacobson was
 about to win a beachhead for a plethora
 of 3M products by buying the sponge
 unit of France's Chargeurs, the French
 government blocked the sale on anti-
 trust grounds.

Jacobson is also starting to insist that
 3M's divisions develop bigger-ticket
 products. The company has been taking
 core technologies and coming up with
 hundreds of variations. But those mar-
 ket niches can be pretty skinny—often
 only a few million dollars or so. Now the
 company's strategists are focusing on 45
 new product areas, each with \$50 million
 in annual sales potential three to five
 years out. One example: A staple gun
 that replaces pins for broken bones. A
 50% new-product success rate would con-
 tribute \$1.2 billion in sales by 1994 from
 this program alone.

SINCERE FLATTERY. Jacobson's latest
 achievements have yet to be reflected in
 3M's stock price, which has been hover-
 ing in the 60s since the 1987 crash. Ana-
 lysts are concerned that despite the com-
 pany's diversification into health care, it
 still makes about 40% of its sales to the
 industrial sector, so it could get socked
 in a recession. And 3M is still considered
 vulnerable in floppy disks and videotape
 and related media, which account for

about \$800 million

in sales. The unit has been locked in a
 bruising battle with the Japanese for
 years, and lost an estimated \$50 million
 in 1987. While those products finally be-
 came profitable in last year's fourth
 quarter as a result of cost-cutting and
 wider distribution, the area could remain
 a trouble spot. "It's a fragile turn-
 around," says analyst B. Alex Hender-
 son at Prudential Bache Securities Inc.

Other companies would love to have
 3M's problems if its successes came with
 them. Indeed, 3M constantly finds itself
 playing host to companies trying to fig-
 ure out how to be more creative. Mon-
 santo has set up a technology council
 modeled on 3M's, and United Technol-
 ogies has embarked on an effort to
 share resources among its not-so-united
 operations. Eight years ago, Rubber-
 maid Inc. began insisting that 30% of its
 sales come from products developed in
 the previous five years.

While other companies may pick up
 ideas piecemeal from 3M, it would be
 impossible for any big corporation to
 swallow the concept whole. "We were
 fortunate enough to get the philosophy
 in there before we started to grow, rath-
 er than trying to create it after we got
 big," says Lester C. Krogh, who heads
 research and development. 3M has a
 simple formula: Find the Francis Okies,
 and don't get in their way. But for man-
 agers of other companies, large and
 small, that's often easier said than done.

By Russell Mitchell in St. Paul, Minn.

CAN P&G COMMANDEER MORE SHELVES IN THE MEDICINE CHEST?

The consumer giant smells big profits in selling other companies' drugs—and it isn't alone

When you reach into your medicine cabinet for NyQuil, Pepto-Bismol or Motrin, you probably aren't realizing you're getting help from Procter & Gamble. The three brands have been around over two years of the consumer-giant's existence, but they may just be getting started. In a few years, if the company has its way, you may regrow hair on your bald spot, treat your ulcer, and cure your headache with over-the-counter products brought to you by the folks in Cincinnati.

Procter already is one of the largest marketers of over-the-counter drugs in the U.S., with sales of \$1.2 billion last year.

Procter also spent \$800 million companywide last year to research and develop new products. But getting a new prescription drug can take a dozen years or more and can cost \$100 million. Getting a winning Food & Drug Administration approval for OTC status can take even longer. To speed things up, P&G is busily signing partnership agreements with drug companies.

By linking P&G's formidable marketing might with the advances in medicine, the ventures may propel the company into the forefront of the pharmaceutical industry.

BEAUTIFUL MARRIAGE. Now is P&G the only big marketer of OTC drugs in the drug company. On Mar. 28,

Procter announced a 50-50 joint venture with Merck & Co. to market OTC drugs derived primarily from Merck's prescription drugs. The interest of drugmakers and con-

sumers in such ventures reflects an increasing sense that the OTC side of the pharmaceutical industry

grow faster than will prescription sales.

While it will be several years before the J&J-Merck partnership will put any new medicines on the market, the deal is "a beautiful marriage of two titans of the pharmaceutical industry," says Ron Nordmann, a drug analyst with PaineWebber Inc. After the wedding, Merck and J&J will be slugging it out with P&G in arenas that are likely to see some of the fiercest marketing battles of the 1990s.

The first big test of P&G's strategy will come from an agreement

with Syntex Corp. in Palo Alto, Calif. Last September the two companies set up a joint venture to seek approval for an over-the-counter form of Syntex's provera, the No. 4 prescription antiarthritic in the U.S. and the top-selling antiarthritic Syntex sells \$497 million of Naprosyn and related compounds in the U.S. a year. And Geoffrey Place, a P&G senior vice-president who oversees partnership arrangements, points out that unit sales often jump when a drug goes OTC. The 50-50 joint venture ed up \$20 million in sales in November's first year as an OTC drug.

Procter's assistant line & sales manager, John Kline, says that could give a boost to P&G's U.S. health care business, which hasn't grown much lately. "That's good."

Procter already has the marketing muscle to make the most of a drug. The company spends \$150 million a year wide annually on advertising. And Naprosyn, a lasting drug effective against a variety of colds and pains, plays into P&G's strategy as a market leader. Nearly all of its biggest successes, from Crest toothpaste to Pampers diapers, were innovative products for which Procter had strong performance data. And after buying Richardson-Vicks, Norwich-Biotin and Searle's OTC unit since 1982, Procter has a list of sales figures lined up for doctors, whose recommendations have long been a big part of purchases.

Such ventures make sense for a growing number of pharmaceutical firms. Consumers and insurers are becoming more interested in OTC medications, partly because of the steep cost of prescription drugs. And with the prices of many major medicines such as the ulcer drug



P&G'S MEDICAL PARTNERSHIPS

- ▶ Working on new formulations for minoxidil, baldness remedy, and new hair-growth products with **UPJOHN**.
- ▶ Joining **SYNTEX** to market anti-inflammatory analgesics, including nonprescription version of Naprosyn, Syntex' antiarthritic drug.
- ▶ Hoping to sell gastrointestinal medicine Dic-Nol, made by Dutch drugmaker **GIST-BROCADES**, as ulcer treatment.
- ▶ May use technology from **ALCIDE**, a Connecticut maker of disinfectants, in its toothpaste or mouthwash business.
- ▶ Has agreement with **TRITON BIOSCIENCES** and **CETUS** to use Binterferon, a synthetic interferon that it hopes could help fight the common cold.

DATA BANK



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due to expire in the next few generic drugs will pose an ever-rising threat to prescription products. Drugmakers are taking another look at the OTC business, where a well-known brand can keep a franchise alive after exclusive rights have expired. It's a lesson the industry learned from American Home Products Corp.'s sales with Advil, an ibuprofen-based pill that went over-the-counter in 1984. Advil now accounts for half of all ibuprofen, or 11.5% of the \$2.2 billion market for OTC painkillers. It carved out a healthy share because American Home had a two-year start as one of only two companies selling the drug. Similarly, P&G is looking to gain FDA approval for an OTC Naprosyn, a non-steroidal anti-inflammatory drug (NSAID) for which Syntex' patent expires in December, 1988. That could give P&G a head start to create a consumer-brand franchise and might withstand the competition after other companies jump in.

Getting Naprosyn approved as an OTC drug won't be a snap, though. The FDA has clinical data showing that a pro-OTC drug is safe and effective at a recommended dosage. Last year Syntex failed on the required clinical work, and could take two or three years. Naprosyn's good record, most observers feel it would eventually qualify. The dosage will probably have to be reduced, since the FDA looks for the lowest effective strength of any new OTC drug. Another potential hitch: On March 1, the FDA asked makers of a number of pain relievers, including Naprosyn, to inform doctors of the risks of ulcers and gastrointestinal problems, and the FDA required the makers to add a warning label.

ESS CURE? P&G itself has stubbed its toe in the OTC world. Encaprin, a co-antipyrine it launched in 1984, was overshadowed by the ibuprofens that came along at the same time. Still, most outsiders are enthusiastic. "Procter will do it," says Bob Hannan, managing director at Genesis Group, a technology consulting firm.

But a P&G push for Naprosyn would trigger a fierce marketing battle with painkillers, where Tylenol, Advil, and Bayer, and other brands are fighting for shelf space. "Anybody who enters any category where P&G is, or has the potential to be, has to be competitive," admits one rival.

P&G is also looking to become a major player in hair restorers. It has an agree-

ment to work on better formulations of Upjohn's Rogaine, which received FDA approval last year as a prescription baldness treatment. And it has a long-term research agreement with Upjohn to develop additional products using its own expertise with skin and hair.

While most of its partnerships give P&G access to new technology, at least one deal simply gives it an ingredient it already has—but with an important marketing edge. Both P&G's Pepto-Bismol and a European prescription drug called De-Nol contain bismuth. The chemical

controls a bacterium that P&G believes causes ulcers. But industry sources note that consumers are unlikely to treat Pepto-Bismol seriously as an ulcer remedy. So P&G has licensed De-Nol from its maker, Dutch biotechnology company Gist-brocades. As a European prescription drug, De-Nol "is just a more believable story," says an industry veteran. It might also more easily

win approval as an OTC ulcer remedy.

That could help P&G get a running start in what's likely to be a hot race to get OTC ulcer treatments on the market. The first consumer medicine to come from the J&J-Merck joint venture will probably be a version of Merck's Pepcid, an anti-ulcer prescription drug with estimated sales of \$400 million this year. SmithKline Beckman Corp. plans to develop an OTC version of its Tagamet sometime in the next four years, and Glaxo Holdings PLC may be aiming to do the same with its ulcer fighter, Zantac.

As for P&G, some company watchers note that the joint ventures reflect a less-than-stellar recent record on the part of the company's own researchers. P&G's Place argues that the moves are no different from the long-established practice of acquiring outside ingredients and technologies. The surfactant that eventually led to Tide, for example, came from a German company. But with the exception of brands that came with companies it acquired, P&G has never before chosen to market products completely developed by outsiders.

And P&G is busily prospecting for more such deals. "I'd hope we'd continue to be recognized by prescription drug companies as an over-the-counter marketer offering a very real opportunity," Place says. It sounds as if the Cincinnati colossus is coming to admit that it can use a little help from some friends.

By Zachary Schiller in Cincinnati, with bureau reports



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A black and white photograph showing a colony of ants working together to build a path through a white, textured surface. The ants are moving in a line, creating a series of connected tunnels. The path starts at the top left and winds its way down towards the bottom right. The ants are small, dark, and their movement is coordinated, illustrating the concept of collective effort and accomplishment.

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IS IT INFLATION? RECESSION? OR JUST SPRING FEVER?

The outlook for the stock market isn't rosy after the March tumble

It has happened four years in a row: The stock market rallies in January and February, only to fall ill when the weather warms up. This year, the market turned green at the gills on St. Patrick's Day, when the February producer price index showed a 1% gain—a devastating 12.7% annual inflation rate. True to form, the market lost 3.4% in just two days. Now, however, other symptoms are appearing—drops in house sales, car sales, retail sales, and durable goods orders—that make observers wonder if the sickness is recession instead of inflation.

Neither diagnosis is good for stocks. The antidote for inflation is higher interest rates. But with short-term rates already at four-year highs, that would siphon capital out of the equity market. A recession would drive interest rates lower but would also slash corporate profits, thus driving stock prices down more than lower rates would bolster them. Wall Street cannot decide whether inflation or recession is more likely. But it does seem convinced that a "soft landing," where the economy slows enough to let price pressure moderate and interest rates fall but not so much as to drive it into recession, is looking less likely. And that could limit the market's ability to launch a rally this spring.

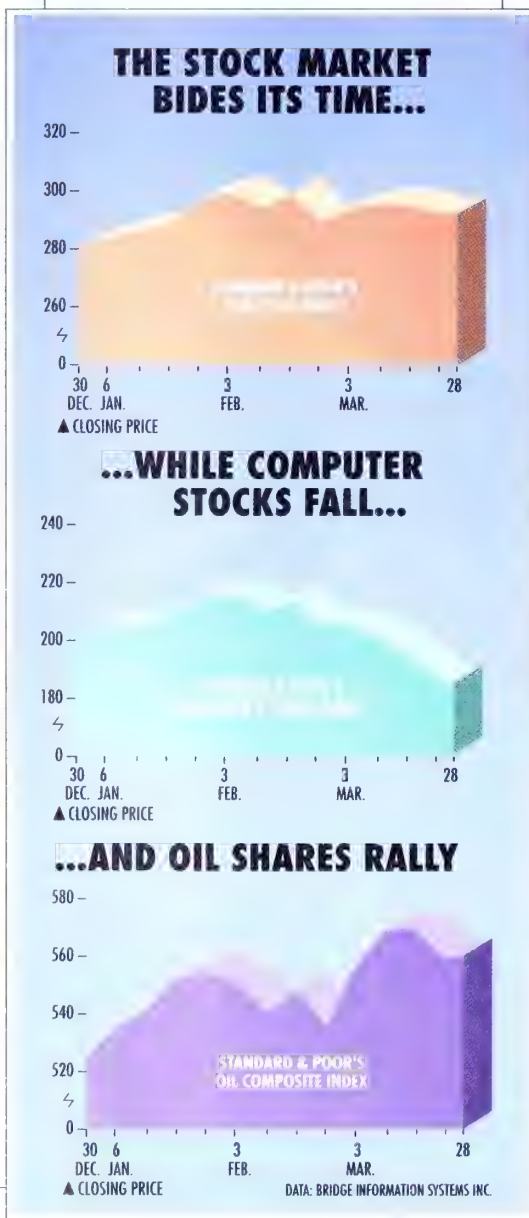
MUDDLED MARKET. Investors can find explanations for both inflation and recession by what is happening in the market itself. Oil stocks, for example, rallied 5% in recent weeks, the only stock group to show much leadership in a muddled market (chart). In the absence of generally rising stock prices, the surge in oil stocks, says Edward P. Nicoski, market analyst for Piper, Jaffray & Hopwood Inc., points to inflation. The 1979-80 run-up in oil stocks was followed by a 1981-82 bear market. But William H. Brown, oil analyst for Kidder, Peabody & Co., says oils have lagged the market in its recent rise and are only now catching up. "This is not the start of a new bull market in oil stocks," says Brown.

Many investors read the sharp fall in computer stocks as proof the economy is tanking. Since early February, Standard & Poor's computer systems index, which includes all major computer companies, has nose-dived 16%. Share prices for such big computer companies as IBM, Digital Equipment, and Unisys are near their October, 1987, crash lows. Rick Spillane, portfolio manager of the Fidelity-Select Technology fund, says earnings problems seem to affect enough companies in the far-flung computer industry to suggest that some macroeconomic forces—such as an economic slowdown—are at work. But more likely, says Spillane, glitches in manufacturing, shortages in software, and quarrels among the industry's players over standardizing computer systems are keeping customers at bay. "I've never heard anyone say they're not going to buy a computer because interest rates are too high," says Spillane.

If oil and computer stocks are sending crossed signals about inflation and recession, the message is the diminished chance for a soft landing is coming across loud and clear. Eric T. Miller, chief investment officer for Donaldson, Lufkin & Jenrette, says the soft-landing scenario is built on the notion that exports and capital spending will remain strong and offset a slump in consumer spending. But there are signs that exports and capital spending are not growing fast enough for that to happen. The surging dollar, a result of high U.S. interest rates, makes it especially tough for exports to pick up speed in coming months.

NO 'BIG FALL.' The Federal Reserve Board sees no reason to loosen monetary policy just yet. To some on Wall Street, this means that a recession is almost a certainty. "To get a soft landing, the Fed would have to start easing up on interest rates right now," says Steven A. Kroll, president of SLH Asset Management. With inflation readings still uncomfortably high, few Fed watchers expect the central bank to turn on the money spigot for several months yet. Merely letting up, says Kroll, is not enough. "If the Fed waits until June, it's going to be too late." At that end, Kroll is recession-proofing his portfolios with food, beverage, drug, soap, and utility stocks—a comfortable 24% cushion of cash.

The uncertainty over the economic outlook has sent many a money manager to the sidelines. Trading volume



as cooled. With one-year Treasury bills yielding 9.7%, a shade less than the average annual return for stocks, money managers have little incentive to make bets. "You're being paid very well to sit tight," says Miller.

Even the strengthening dollar isn't enticing in foreign investors. "We don't see a big fall coming, but we don't see any big gains either," says Olivier Huby, head of U.S. investment strategy at Ribas Asset Management.

Foreigners say they see better prospects elsewhere. The red-hot Japanese stock market, which had dropped about 20% from its February high, has shifted back into high gear. On Mar. 28 the Nikkei average shot up nearly 800 points and followed with 431 points on Mar. 29, to reach a new record of 32,737. Kenneth Courtis, senior economist at DB Capital Markets (Asia) Ltd., predicts flat out for the Japanese market will climb to 40,000 this year. "Savings and liquidity are growing," he says. "And we're looking for good economic growth."

SH RICH. Although investors are cool toward U.S. stocks right now, the Dow Jones industrial average, at 2282, is generally expected to remain north of 2100. Why? There's plenty of cash around, and investors still indicate they're willing to go bargain hunting when prices drop. W. Thacher Brown, president of B&B Investment Advisors, says many stocks are so cheap they already incorporate an economic slowdown.

There is some encouragement, too, in the public's improving confidence in stocks. Neal Litvack, vice-president for marketing at Fidelity Investments, says he's surprised that of all the equity mutual funds his company offers, the risky Fidelity International and Capital Appreciation funds are attracting the most new accounts.

Stock prices will get further support from the still-active takeover and leveraged-buyout game. New deals pop up almost every day. Takeovers and corporate stock repurchases are expected to mop a floor under the market by shrinking the supply of equity. That's what keeps money manager David Elias bullish. "The smart money is still buying," says Elias, who has some 80% of the \$100 million under his management in high blue chips as Eastman Kodak, McDonald's, and Walt Disney.

Laszlo Birinyi of Birinyi Associates is also bullish. The current weakness, he says, is merely the market consolidating after a 13.6% rise since the middle of November. "We go through these end-of-the-world crises every once in a while," he says. But with the economy struggling with high interest rates and a business slowdown, this time the jitters may be justified.

By Jeffrey M. Laderman in New York, with bureau reports

HOW THE UNBUNDLED UNIT CAME UNBUNDLED

Shearson dumps the project, citing an SEC objection

It was no great secret on Wall Street that Shearson's Unbundled Stock Unit (USU) was in trouble. But when Ronald L. Gallatin, a managing director of Shearson Lehman Hutton Inc. and the father of the USU, told a meeting of the National Association of Treasurers on Mar. 28 that the USU was dead, the audience was stunned. After Gallatin read them the press release, "to suggest there was a little silence in the room is an understatement," he says.

Shearson revealed that the Securities

The earnings question was not known to be a major stumbling block to the USU innovation; other factors seemed to loom larger. Outraged shareholder groups wrote the SEC protesting that the USU took away investors' voting rights. Institutional investors, whose support was crucial, doubted that the broken-up securities would be worth more than the one original share, and seemed reluctant to exchange their shares. Shearson eventually brought in Goldman Sachs & Co. to help market USUs to the institutions. The

earnings dispute "came out of left field," Gallatin says, because the talks between Shearson and the SEC were private.

HIGH HOPES. Shearson had great expectations for the USU. In the beginning it hoped to reap \$95 million in investment banking revenues from USUs. The plan to carve up a share of stock probably received more initial publicity than any other financial concept in recent memory. It all started on Dec. 5 when Shearson, with great fanfare, announced that four blue-chip companies—Dow Chemical, Sara Lee, Pfizer, and American Express, which owns 61% of Shearson—had agreed to swap up to \$5.6 billion of their stock for the unbundled securities.

Now, Wall Street experts are fretting that the USU flop will discourage securities firms from marketing new

ideas. Their industry—which has had little luck selling stocks to individuals since the October, 1987, crash—desperately needs to develop revenue sources.

Investment experts are glum about prospects for other ideas. "Wall Street firms are now going to take a long, hard look at the new products in their pipelines," says Leslie C. Quick III, president of Quick & Reilly Group Inc. Adds PaineWebber Inc. analyst Brenda D. McCoy: "The end of the USU is a further indication that the rapid growth of new products is not going to continue."

By Jon Friedman in New York, with bureau reports



GALLATIN: THE FATE OF HIS IDEA MAY DISCOURAGE OTHERS FROM MARKETING NOVEL INVESTMENTS

& Exchange Commission's chief accountant, Edward Colson, clashed with Shearson over the radical plan designed to have companies redeem up to 20% of their shares and divide each share of stock into a bond, a share of preferred stock, and a warrant. Supported by five major accounting firms, Shearson had argued that after the swap, profits could be spread across fewer shares and thus boost the issuing companies' per-share earnings. According to Shearson, the SEC insisted that in calculating earnings per share, the number of USUs must be added to the total of shares outstanding. The SEC has declined comment.

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ANNUAL REPORTS: THE SEC CRACKS THE WHIP

Pushing hard for more candor

It's spring: a time of cherry blossoms, baseball, and, to really lift the spirits, annual reports. From the cheery president's message in front to the financial ruminations in back, the reports are notorious for accentuating the positive and soft-pedaling the negative. But the Securities & Exchange Commission is beginning to cast a skeptical eye on this corporate ritual.

After years of letting the issue sit on the back burner, the SEC is issuing a set of guidelines aimed at requiring franker discussion of a corporation's health and prospects. The new rules, expected out in a few weeks, will focus on what many investors consider the heart of these reports—the Management Discussion &



Analysis (MD&A), a compact dissertation on corporate operations that is required in the Form 10-K filed with the commission and usually included in the glossy annual reports that shareholders get. "It's fair to say improvement is needed," says Howard Morin, assistant director of the SEC's Corporation Finance Div.

MONEY & BANKING

CAN THIS FLIGHT BE GROUNDED?

The exodus of capital from the big debtor nations looks unstoppable

Condos in Miami. Factories in California. Swiss bank accounts. All represent money that has fled Latin America's political instability and ruinous economic policies. With citizens of the 15 largest debtor countries now holding at least \$340 billion in "flight capital" abroad, Treasury Secretary Nicholas F. Brady says winning some of this treasure back would be a "major opportunity" to ease the Third World debt crisis. But when Brady's recent debt-reduction plan is debated at the International Monetary Fund session in Washington on Apr. 3, his capital-flight ideas are likely to get short shrift.

Some tough approaches already have been scuttled. Brady broached slapping a withholding tax on Latins' accounts in U.S. banks. But the Federal Reserve Board blocked the plan, arguing it would cost American banks business. Brady then suggested that debtor nations be required to fill some of their foreign fi-

ancing needs by reclaiming flight capital. But the debtors see this as meddling. "Limits on market movement of private money would be very cumbersome, counterproductive, and contradictory," objects Brazil's ambassador to Washington, Marcello Marques Moreira.

LOADS OF LOOPHOLES. Even if new controls were imposed, Latins wouldn't take long to evade them. In Brazil, trading firms routinely doctor export and import invoices to get extra dollars from the central bank. In other Latin countries, no sooner do foreign loans arrive than some of the proceeds suddenly show up in bank accounts in Miami or Zurich. And while international banks express mild concern, they can't get enough of flight capital. A phalanx of foreign banks and brokers is doing a land-office business in São Paulo, Caracas, and other big cities, discreetly offering "private banking" services to rich people seeking opportunities abroad.

Latin governments could, of course, keep some potential flight capital at home by improving the fundamentals—cutting inflation, devaluing currencies, boosting interest rates, and selling state industries. "If the signals are right, capital won't fly," says Norman R. Klath, a

That's putting it mildly. In a last year, the SEC scrutinized the 218 annual reports, mostly for 1987. The results were startling: Only a few companies passed the first review. Some were so misleading that they were referred to the SEC's enforcement staff, while more than 70 companies were ordered to amend their filings. A review of 141 companies is under way.

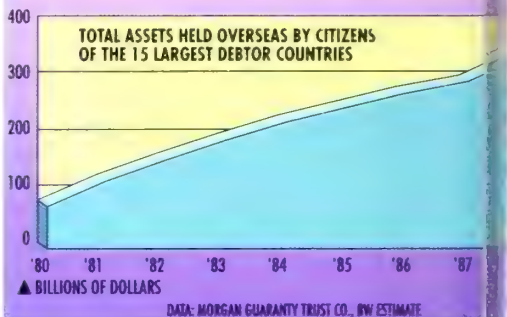
LOW COMPLIANCE. Critics in Congress and the financial community have charged that the SEC has done a poor job of overseeing financial reporting, especially in such problem areas as the savings and loan industry. In the 1970s, the SEC imposed a "percentage test" which companies had to discuss earnings that changed revenues by 10% or more. But in 1980 the SEC did away with the test and instead called for more focus on future trends. But managers still pulled their punches. "The level of compliance has gone down," says Stephen H. Lewis, a New York securities lawyer.

Managers have argued that the SEC's few hard-and-fast guidelines on what to include in the management analysis. But if the SEC pursues the MD&A with vigor, that excuse won't fly anymore.

By Tim Smart in Washington

Morgan Guaranty Trust Co. vice president. But others say industrial nations can do as much to raise confidence. "If the U.S. creates more optimism about what's going to happen on debt, that will do more to stop capital flight than any direct measures," says Jacques J. M. senior adviser to the Organization for Economic Cooperation & Development.

MONEY IS FLEEING THE THIRD WORLD



Brady, like many Americans, can help but seethe at the prospect of losing money abroad. But capital repatriation isn't the solution to the debt crisis. It will be the Third World's reward for getting its debt down and its economy on a running.

By Mike McNamee in Washington
Jeffrey Ryser in São Paulo

ELECTRONIC BANKING MAY HAVE TO LOG OFF

band is so slim that many banks have already unplugged

When home banking via personal computer made its debut six years ago, banks heralded the greatest invention since the sit slip. Citicorp, Chase Manhattan, Chemical Banking invested huge. With the PC boom, the banks figured millions of well-heeled customers would happily pay a premium to avoid cash checks and visiting branches.

It was the dream. But today banking by PC is in trouble and may not survive unless the banks find partners who bring the latest communications technology to bear. Only 36 banks offer service, down from 70 several years ago and 100,000 people subscribe to the programs—a tiny fraction of the 28 million households that have personal computers. Even some of the pioneer banks are pulling out. After five years and outlays that analysts put at \$100 million, Pronto service introduced by Chemical Bank and American Telephone & Telegraph closed down on Jan. 31. And in January, Chase Manhattan scaled back its year-old Spectrum and doubled its monthly fee to \$10 from \$5. "In the five to ten years there will be much greater demand for electronic banking services in the home," says John W. Barab, a Chase vice-president. "The near

future is a little more hazy." But it may stay that way. Alternatives are proliferating, including inexpensive telephone banking services that give round-the-clock account balances and provide rate information to users of computer-based banking services such as Minitel, AT&T TeleCom in New York and CheckFree in Columbus, Ohio. "Customers still see banking as something more beneficial to the bank than it is to them," says Gary Arlen, president of Arlen Communications Inc., a research firm in Bethesda, Md.

ABLE FLOAT. Clearly, the bankers are enjoying any benefits in the electronic service. The monthly fees provide a steady, reliable revenue source. Citi, one of the few major banks still gaining home-banking customers, sees enormous potential economies for itself in checking time and labor. Subscribers who are devoted users tend to be afflu-

ent and are likely to consolidate all their accounts at the bank. And they tend to maintain sizable balances, so the bank gains valuable float; the bank debits a customer's account immediately but often has use of the funds for several days before passing them on. Citi's 40,000 PC-banking customers "are extremely profitable," says Anne Slattery, vice-president of product marketing.

Some banks may resurrect home



Of 28 million households with PCs, only 100,000 subscribe

banking by linking up with the regional Bell operating companies. They won permission last year to become "videotex gateways" and can now provide electronic mail, voice mail, billing management, and data transmission over the telephone. Joshua Harris, president of Jupiter Communications, a New York research and consulting firm, predicts that banks and Baby Bells will emulate the French telephone system, which gave away simple low-cost Minitel terminals to 3.5 million households in 1977. French subscribers use Minitel to access their bank accounts as well as information and shopping services. Bell Canada is now experimenting with a similar terminal in Montreal.

Sears, Roebuck & Co. and IBM are hanging in for the long haul. The retail-

ing giant and Big Blue have invested some \$400 million in Prodigy, a videotex service. For \$49.95 worth of software and \$9.95 a month (plus phone costs), it offers home banking as well as shopping, airline reservations, news, and games. Although Prodigy says it has tens of thousands of subscribers, its backers expect no profits for another 10 to 15 years. "We like to say we're shooting ahead of the duck," says Prodigy spokesman Geoffrey Moore.

'CLASS MEDIUM.' If Prodigy thrives, many more people will be exposed to electronic banking. The service's software package is Manufacturers Hanover Corp's Excel. Manny Hanny, with 6,000 Excel users of its own, has licensed the program to five regional banks linked with Prodigy, and they in turn have enlisted another 2,000 customers. A direct-mail solicitation brought Citizens & Southern National Bank in Atlanta a 7%

response rate, twice the average reply, according to Bruce Bellmare, Prodigy's director of bank marketing.

If Prodigy does succeed, it will do so in an industry where many others have failed. Knight-Ridder Inc. and Times Mirror Co. spent tens of millions on videotex projects that eventually folded in 1986. Sears, IBM, and Citibank have the deep pockets to absorb such losses. And unlike Chemical and Chase Manhattan, they aren't under pressure to build capital and dispose of projects that aren't immediately profitable. But banking by PC is still perceived to be an indulgence—"a class medium, not a mass medium," says Arlen. Unless the banks move quickly to make the service more rewarding for their customers, the home-banking elite may remain a very small class indeed.

By Laura Zinn in New York

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THE MONEY MAGICIAN AT PHILIP MORRIS

CFO Hans Storr is the unsung hero of the Kraft takeover

When the smoke cleared after the \$25 billion leveraged buyout of RJR Nabisco Inc. last fall, none of the gunslingers in the takeover shoot-'em-up walked out a hero. But while the RJR crowd was firing at each other, another blue-chip giant was proving that tobacco-food takeovers can be done quickly and smoothly. Philip Morris Cos.' \$12.9 billion acquisition of Kraft Inc. in October went like clockwork.

A lot of the credit goes to the unsung hero of the deal, Hans G. Storr, Philip Morris' chief financial officer. Within 24 hours of the hostile bid's announcement, banks around the world had offered him more than \$19 billion. Then, convinced that interest rates were headed up, he locked in rates of less than 10% on half of the \$9.6 billion in borrowing needed to buy Kraft. "The key to the deal was financial flexibility," says investment banker Bruce Wasserstein of Wasserstein Perella & Co., which advised Philip Morris on the deal. "By raising money quickly and keeping the cost of capital low, Hans did a terrific job."

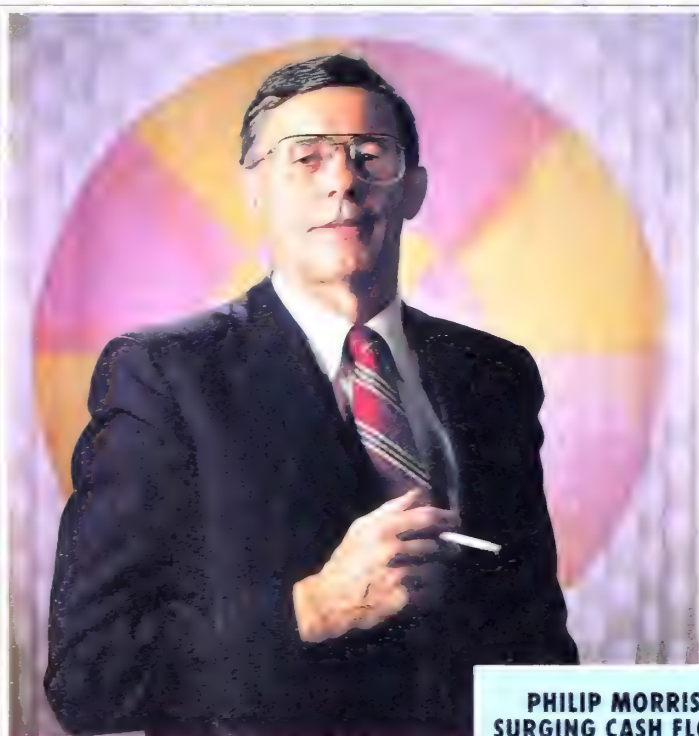
Storr, 57, is such a company man that he encouraged a visitor to his Park Avenue office to take up smoking. And he is used to having his CEO and 23-year colleague, Hamish Maxwell, command the spotlight. Yet Storr is one of the top four decision-makers at Philip Morris, and he is a top gun among CFOs.

MARKED FOR LIFE. In that role, Storr is best known as a deft forecaster of currency fluctuations. In late 1984, figuring the U.S. trade deficit would soon undermine the dollar, he began shifting \$2 billion into foreign currencies. Riding them up for the next three years made \$400 million for Philip Morris.

Storr's affinity for international finance has a lot to do with his European roots. He was born and raised in Germa-

ny. He remembers rummaging through the attic of his family home and finding musty records of his father's bankrupt business, which was wiped out in the Depression, and bundles of German marks rendered worthless by runaway inflation. "It left a tremendous impression on me as to what is value."

Leaving war-torn Europe for Wisconsin, he became an accountant. Later he



STORR: HE HAD \$19 BILLION LINED UP WITHIN 24 HOURS OF THE KRAFT BID

went to Korea as a G.I. and then joined a former unit of Philip Morris in 1957.

In addition to his long-term perspective, Storr has a keen sense of limits. Once, at a meeting of senior managers held in Nigeria, he donned an African mask and waved a carved wooden snake to make a point about the mysterious nature of exchange rates: "The CFO's role is like that of a shaman, a magician, where the outcome is similarly unpredictable. There is nothing scientific about it."

All any CFO can do, Storr says, is form an opinion on the major trends and monitor their currency risk closely or diversify. Right now, Storr expects the dollar to strengthen as the prime rate climbs from 11.5% to 12.5% by year's end.

Storr's greatest challenge now is to make sure Philip Morris' shareholders benefit from acquiring Kraft. Typically, an acquiring company's stock slides if the buyer struggles to digest its acquisition. Only when a company is the object of a bidding war is its stock apt to double in a matter of weeks, like RJR's did. Philip Morris stock is already up, too, from its November low of 91. His shareholders could do as well as RJR holders says Storr, provided they have patience. "In the next few years, we will have the same kind of appreciation as RJR shareholders had and still have great prospects for further appreciation."

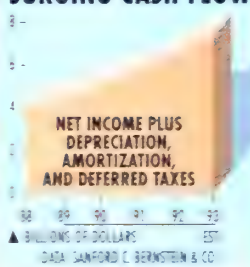
Some Wall Street analysts expect the stock price to range from \$145 to \$175. These estimates are based on Philip Morris' strong cash flow, largely because its cigarette business is so profitable. Over the next five years the company expects to produce about \$1 billion in "free cash flow," basically the amount of earnings management after paying for capital expenditures and dividends. Only five companies, including IBM and General Motors Corp., generate more cash.

This stream of free cash flow has allowed Storr to leverage Philip Morris' balance sheet to \$16.4 billion, for a debt-to-equity ratio of 2.1 to 1. He should be able to pay down \$9.6 billion in Kraft debt in only four years.

But all of Storr's financial savvy won't matter unless the diversification works. He played a major part in shaping the strategy, and it is the biggest of his career. At stake is whether Philip Morris can escape the stigma of being a tobacco company and be valued by the market as a food company that just happens to have a rich and certain cash flow. It's up to Storr to finish the job of convincing Wall Street's witch doctors that some things after all, are predictable.

By Leah J. Nathans in New York

PHILIP MORRIS' SURGING CASH FLOW



GENE G. MARCIAL

ILL JAPONICA AG A RAILROAD— R GET DERAILED?

Jo, Japonica Partners has no connection with Japanese investors. It was formed last year by two ex-Goldman Sachs merger-and-acquisition pros, Paul Kazarian and the Lederman, and it is drawing the set's attention because of its surprise attack on the old-line railroad financing company, CNW.

Japonica's Mar. 13 disclosure that it is an 8.8% stake in CNW accelerated the rise of the stock to nearly 40 from 25 in January. But lately CNW sagged to 37, largely because of fights among arbitrageurs that Japonica is a fairly new kid on the takeover block, can mount a serious assault. Take no mistake: Japonica is dead serious about acquiring CNW, which operates a 6,400-mile Midwestern railroad system that transports grain, cars, oil, and coal and has revenues of \$1 billion. Kazarian and Lederman have been on CNW's board that they'll seek control. Japonica will soon make a tender offer, says a takeover adviser familiar with Japonica's strategy. "Our goal is to pump up the stock or extract cash. We want to own the company," says one of Japonica's partners.

Several banks and financial institutions "have eagerly offered to participate in financing a deal," he says, "and we are now in deep discussions with Japonica." It's possible that Japonica will first increase its stake in CNW to as much as 14.9% before making a bid. They want 15%, they must file with the Federal Trade Commission. Right now, though, the group already has equity necessary to get the financing for a takeover bid.

GILE REPRIEVE. Kazarian and Lederman are familiar with CNW's operations and assets and how much they might fetch. Kazarian was investor in Haley's adviser when Haley launched a proxy fight for control of CNW last year. The effort was aborted when CNW agreed to be acquired at \$31 a share by a group consisting of several CNW officials and Gibbons, Green & Amerongen, a leveraged-buyout investment firm. But that deal fell apart in April. Since then, CNW Chairman Herbert Schmiede has said that the company will fight to remain independent. But he and other officers own

CNW COMES OFF ITS HIGH



little of the stock, while institutional investors hold about 35% of the 18.6 million shares outstanding.

Kazarian and Lederman insist that management has failed to close the "value gap" that exists in CNW's stock. Frank Gallagher, a director at Phoenix Capital Markets, values CNW's assets at \$2.042 billion. Subtracting debt and preferred stock of \$843 million, Gallagher pegs CNW's net asset value at \$1.2 billion, or \$64.25 a share.

Gary Yablon, an analyst at Oppenheimer, says CNW's most attractive asset is Western Railroad Properties, the coal-hauling line that he figures is worth more than \$35 a share. "So at the stock's current price, the market assigns only about \$2 a share for the rest of the company," he says, adding that Japonica's bid could well encourage other interested parties, including Union Pacific Railroad and Conrail.

INFRARED HAS OPTEK GLOWING

When Optek Technology, a small Texas company, gobbled up a TRW unit three times its size, it emerged as the leader in the little-known optoelectronics business. Analysts say its stock, currently at 7, could double in a year.

Optek makes custom infrared electronic products that are found in homes, cars, and hospitals. Devices that emit and sense infrared light are used to open and close garage doors, work TVs and VCRs by remote control, track automobile speeds, and control the flow of intravenous fluids that are administered to hospital patients.

Optek's July, 1988, acquisition of TRW's optoelectronics division for \$32.6 million boosted Optek's revenues from 1987's \$14.2 million to \$28.7 million last year. And earnings jumped from 1987's \$708,000 to \$942,000, or 30¢ a share, in 1988. But this year's leap may be even bigger. Revenues are expected to hit \$64 million, with earnings of \$2.4 million, or 70¢ a share.

Optek expects to sign a contract with a major auto maker soon to produce a component to replace the distributor in the ignition system. "Investors have yet to fully realize how undervalued Optek is and how much it has changed in the past year," says Richard Davis, an analyst at Rauscher Pierce Refsnes.

LOUISIANA-PACIFIC'S ACRES OF ASSETS

Louisiana-Pacific isn't on many buy lists these days. Some 80% of the forest-products company's output is meant for construction, an industry in a slump. A big producer of lumber, plywood, pulp, and other wood products, Louisiana-Pacific is expected to post earnings this year about the same as last year's \$3.54 a share.

Even so, several pros have been accumulating the stock, currently at 30, as an asset play. Despite the dismal fundamentals of the lumber business, the company has repurchased about 1.5 million shares in the past six months.

Scott Black, president of Delphi Management, is among those who have been snapping up shares. "If there is an asset-rich company that would be easy prey to a takeover raid or an LBO," he says, "it's Louisiana-Pacific, with an estimated book value of \$29.50 a share." He puts the company's LBO, or breakup, value at \$43 to \$48 a share. Black notes that L-P is practically debt-free, with cash on hand of about \$256 million. The company controls about 3.5 million acres of timberland in eight states, mostly in California, Louisiana, and Oregon.

One big investor says management is aware that the company is a "sitting duck for the raiders." He says that Chairman and President Harry Merlo has told several investors that if an outside group puts the company in play, a management group stands ready to do an LBO. A company spokesman says L-P had been rumored to be a buyout target, but nothing is going on. He adds, though, that an LBO isn't out of the question if it becomes necessary.



**NORMAN AND
JOBS: A \$100
MILLION DEAL**

COMPUTERS

STEVE JOBS GETS THE KEYS TO THE OFFICE PC MARKET

He has a new link with Businessland—but daunting rivals

When Steven P. Jobs introduced his new personal computer and his new company, Next Inc., last October, no one really believed that Next would be content as a small competitor in the \$1.5 billion-a-year U.S. campus PC market. Skeptics thought that the co-founder of Apple Computer Inc. really had his sights on the \$15 billion office PC market. They were right. Now, Jobs has reached a deal with the Businessland Inc. chain of computer stores, which will buy at least \$100 million worth of his computers in the next 12 months to sell to companies.

That will give Next one of the fastest starts in computer history—and possibly a lead in a new phase of personal computing. In the 1990s, industry experts expect businesses to replace conventional PCs with faster desktop computers. Such machines will have the sophisticated graphics and networking capabilities of technical workstations, the powerful microcomputers that Sun Microsystems, Apollo, Hewlett-Packard, and Digital Equipment now sell to engineers. These companies—and perhaps a well-heeled Next—could thus become significant rivals to IBM, Apple, and Compaq. "It's a

new industry out there," says Sanford C. Bernstein & Co. analyst Mark D. Stahlman. "Next could become a world-class shipper in the early 1990s."

To do that, Next needs Businessland. Development snags delayed Next's rollout by 18 months. And thus far its salespeople have sold only 1,000 machines to software writers and universities. So now it needs to move fast. "We wanted one great partnership," says Jobs. "We're putting all our effort into this one." Businessland Chairman David A. Norman says he'll take delivery of the full order, even if the machines don't sell.

EXCLUSIVE DEAL. It's a good gamble. The \$1.2 billion chain, a major supplier to large companies, has at least a one-year exclusive deal. Even if the \$10,000 Next machine isn't a best-seller, Businessland will learn a lot about workstations. The chain is widely expected to carry IBM workstations, too. "We need to get in on the ground floor,"

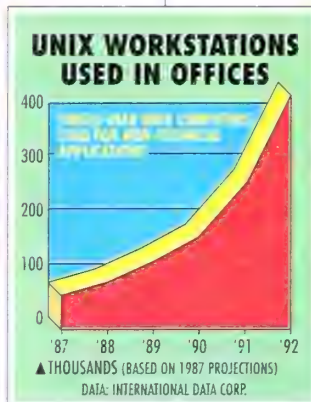
says Norman. Compaq Computer Co. recently pulled its machines out of stores. And Sun Microsystems Inc. spurned him, saying its customers would rather buy direct.

Norman's strategy is to make Businessland an even bigger installer of workstations, probably the most lucrative future market for desktop computers. Workstation makers say their machines are best for that because their software is the Unix operating system, which lends itself to networking. Norman agrees: He's betting that by 1992 Unix workstations will account for 15% of office PC sales vs. an estimated 5% now. Businessland has doubled its staff of technical specialists to 800 in the

three years. Now, Next is training 130 of those specialists in the intricacies of workstations.

OVERKILL? Norman may be too optimistic. Jobs has proven yet that offices need workstations. "I wouldn't bet the race on it," says Edward Anderson, chief operating officer of Compaq Land Corp., a Businessland competitor. And Lynn Johnson, manager of workstation computing

at Boeing Computer Services: "Office workers don't need all that power." Market researchers at International Data Corp. say all that is changing. They are raising their original 1987 projections of sales of workstations in offices (chart). Nevertheless, the researchers project much slower growth than Norman



MEAD TRIES A NEW-FANGLED MEDIUM: PRINT

The on-line data giant wants to diversify beyond Lexis

Jack W. Simpson usually has a subtle sense of humor. But the president of Mead Data Central Inc. got a little blunt recently. Last December, when parent company Mead Corp. shelled out \$226.5 million for Michie Co., a small legal publisher with annual revenues of just \$34 million, Simpson sent the parent company's chief of corporate strategy a stuffed dog. The canine, flashing a toothy grin, was carrying a note that asked: "You paid what for Michie?"

It's a logical question. Bruce Kirk, an analyst at Goldman, Sachs & Co., sums up the Michie acquisition from MacMillan Inc. in three words: "Dilutive, dilutive, dilutive." Still, although the deal will lower Mead's 1989 share earnings by about 25¢, Simpson now says he has no regrets. That's because little Michie has emerged as a key part of an ambitious attempt by MDC to outgrow its image as a one-note electronic publisher. And Simpson is the chief cheerleader for this strategy. "We don't want to be pushed out of publishing" because we are too narrow, he says. "So we're hedging our bets."

COLLISION COURSE. MDC's name is synonymous with Lexis, the on-line legal data base that is the company's cash cow. Lexis, which provides electronic, full-text copies of federal statutes, case reviews, and other legal information, largely fueled the company's record 33% growth last year, the sixth straight year that MDC's revenues rose by more than 20%. What's more, Lexis accounted for \$215 million of Mead Data's \$307.6 million in 1988 revenues, according to research



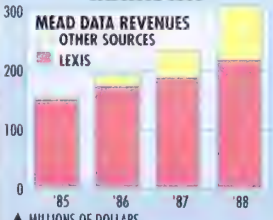
PRESIDENT SIMPSON: "WE'RE HEDGING OUR BETS" WITH MICHIE

firm Amidon/Litman Associates Inc.

Trouble is, Lexis has been around for 16 years. And despite its best efforts, MDC, based in Miamisburg, Ohio, has been unable to come up with another product that does as well. For instance, Nexis, an on-line data base of newspaper and magazine articles, is frequently criticized for being difficult to use and hasn't attracted a huge following. Now, Michie is Mead Data's first attempt at diversification outside of electronic publishing. Michie sells statutes from 23 states, in printed form, to law firms, courts, corporate legal departments, and electronic publishers. Mead Data plans to jack this up to 50 states before long.

This strategy puts MDC on another collision course with its old nem-

LEXIS IS MEAD DATA'S MAINSTAY



if he's right, Next faces daunting competition. Sun, HP, IBM, and DEC bring their workstations at the market. In April, Sun plans to launch an under-\$10,000 model. What makes such machines a hit is workstations software that's superior to that of PCs. At this point, however, MicroCorp's OS/2 operating system for PCs is the one most software developers are writing programs for.

FARE DEARTH. For Jobs, this may be like déjà vu. When his team at Apple introduced the Macintosh in 1984, it had little software. As a result, many businesses refused to buy it. For nearly two years, college students and computer hobbyists kept the Mac going until the machines were sold to arouse interest of major business-software makers.

Following this, Next's engineers developed their machine to work with an object-oriented computer language that simplifies programming. Apple Corp., whose PageMaker publishing software helped make the Mac a hit, is competing for Next. "Our engineers are able to do more in a shorter time on the Next machine than with any other," says Aldus President Paul Erd.

Next also has commitments for software from Lotus, Novell, and Frame Technology, another supplier of desktop publishing software. These packages, along with Businessland's marketing and the half-dozen programs that run on Next machines, should create enough momentum to attract other software developers, says Jonathan W. Seybold, publisher of *Seybold Reports*.

Next also will get a boost from a licensing agreement Jobs worked out last year with IBM Chairman John F. Akers. It gives rights to use NextStep, the company's graphics software and prompting system. Akers says that NextStep will appear on IBM's Unix machines this summer. When that happens, software developers will be able to write programs for Next that can be easily ported to IBM—and vice versa.

Obviously, Next still has a lot to do. Developing an operating system for its machine will not be completed until the end of 1989—after it starts shipping to Businessland. And the company hasn't proved at its automated factory will be able to crank out computers quickly and cheaply. Moreover, the optical disks that computers use instead of floppies add an oddity that may slow customer acceptance. Yet if Jobs can deliver all that he says he will, Next could become a strong influence on computing in the 1990s. For now, at least, it has made all the right moves.

Richard Brandt in Palo Alto, Calif.
Maria Shao in San Francisco

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esis, West Publishing Co. West sells Westlaw electronic retrieval service legal documents. With \$350 million annual revenues, West also rules the field of legal text and research books. For years, MDC and West battled copyright infringement and antitrust claims for their electronic products, racking up litigation costs that Simpson says "would stagger a grown elephant." Last July the two finally settled a licensing agreement that lets MDC use West-copyrighted printed information over Lexis. This time West could end up in the driver's seat again, considering its tenfold revenue advantage over Mead. "We're glad Mead has finally recognized that there's more to legal publishing than on-line data bases," intones Thomas J. McLeod, Westlaw's manager of sales and government relations.

Still, Michie may be good for Mead. Simpson intends to use its staff to upgrade Lexis offerings by writing annotations on court decisions. Then he hopes to add the improved Lexis and a more inclusive database. Michie will make customers take note of MDC's other non-Lexis ventures.

SMALL MONEYMAKER. Among them is Mead Data partnership with a Ford Motor Co. subsidiary, EDM, to build an Electronic Data Gathering & Retrieval system (EDGAR), a public on-line database of Securities & Exchange Commission filings. When EDGAR is completed in four years, Mead Data will sell subscriptions, tentatively pegged at \$240,000 a year, to electronic publishers such as Dow Jones News Retrieval and Dun & Bradstreet Information Systems. EDM will never be a big moneymaker—Simpson says it will bring in no more than \$1 million a year in sales.

But MDC hopes to be seen as the "central" source of SEC information. The plan is to win more financial and corporate customers for its Lexis Financial Information Service, a sputtering Lexis spin-off that provides stock quotes and securities analysis. Once EDGAR is on line, Simpson also plans to work on a new delivery system for all MDC products. For instance, a 1985 acquisition, Micromedex Inc., already sells information about poisons and emergency medicine on compact disks, which are much cheaper to provide than on-line distribution.

It's an ambitious plan. With more acquisitions and new products, Simpson expects MDC's revenues to reach \$1 billion by 1993. But for that to happen, Michie will have to accomplish what Mead Data has been unable to do for itself so far: overhaul its image as little more than a provider of on-line legal data. If Michie can do that, even Simpson will say it was worth the money.

By Maria Mallory in Miami

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FUSION IN A BOTTLE: CAN IT BE THAT EASY?

It sounds unlikely, but then again, so do all breakthroughs

They did it with the kind of equipment that high school chemistry students use to break up water into hydrogen and oxygen—a glass jar for the water and a couple of wires hooked up to a car battery. But B. Stanley Pons, chairman of the University of Utah's chemistry department, and his former teacher, Martin Fleischmann, professor of electrochemistry at England's University of Southampton, say they have turned that table-top experiment into the world's first sustained nuclear-fusion reactor.

Just before Easter weekend the two scientists told a jammed Salt Lake City press conference that their simple apparatus could mark the end of a decades-long quest to harness the reaction that powers the sun—promising a virtually unlimited supply of cheap, comparatively clean power in the 21st century. The concept, said Fleischmann, “will be relatively easy to make into a usable technology for generating heat and power.”

HEATED REACTION. Not surprisingly, such an unorthodox announcement coming from a pair of chemists drew heated—and highly skeptical—reactions from physicists who have been trying to develop fusion reactors for more than 40 years (box). When scientists call a press conference, says Robert L. Park, professor of physics at the University of Maryland, a research paper is usually available to back up any claims. “They didn’t provide any real information,” he notes. Says Donald L. Correll, a physicist working on fusion at Lawrence Livermore National Laboratory: “I still don’t have an understanding of what these guys did—and they don’t either.”

Pons and Fleischmann aren’t dismayed by that response. At the press

conference Pons admitted that even he and Fleischmann initially thought success was a billion-to-one shot. Since they figured nobody would cough up any money, they paid for the experiments themselves, ultimately chewing up nearly \$100,000 over five years. As for the unusual press conference, a spokesman for the University of Utah says it was called because rumors of the discovery were spreading around campus and

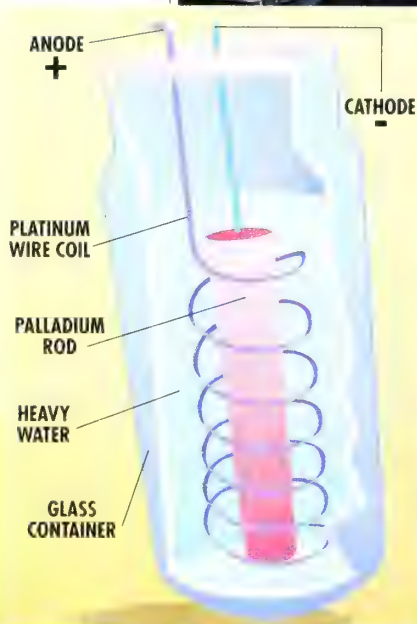
because the simple hydrogen atoms of water are replaced by deuterium, a form of hydrogen whose nucleus contains a neutron in addition to the usual proton. The chemists also replaced the jar’s common electrodes with more exotic conductors: a platinum-wire coil wrapped around a palladium rod and

Connecting these to a car battery separates the heavy water into deuterium and oxygen. Because the resulting deuterium ions have a positive charge, they migrate to the palladium rod, where they’re absorbed. After several hours, say Fleischmann and Pons, the palladium’s crystalline structure becomes densely packed with deuterium ions, which begin to fuse. In the process, energy is released in the form of heat—more energy than they put into the reaction as electric current.

Indeed, Fleischmann and Pons became convinced that their electro-



Pons and Fleischmann with their fusion flask. It packs ions from heavy water into a palladium rod, where, they say, fusion occurs



Why the paucity of detail? One, to avoid jeopardizing the university’s patent application, and two, Pons and Fleischmann didn’t finish a research paper intended for the British journal *Nature* until the day after the press conference.

What Pons and Fleischmann did reveal are the adjustments they made to the usual high school electrolysis experiment. Instead of ordinary water, they use “heavy” water—the same stuff that fuels some nuclear reactors. It’s heavy

cell was triggering fusion when they tried turning up the juice flowing from the jar. The palladium promptly melted, which takes a temperature of about 3,000°F. Producing that much heat from the current from a car battery, says Pons, “can only be accounted for by clear reactions.”

If Pons and Fleischmann have really bottled fusion, they owe an intellectual debt to F. C. Frank. He laid the basis for “cold fusion” in 1947 at the University of Bristol in England. Frank theorized that if subatomic particles called muons could be substituted for the electron-

en atoms, the size of the atoms—
 air repulsive force fields—would
 enough to allow the atoms to
 together, and fusion could occur
 temperatures. Otherwise, fusion
 tremendous heat to overcome
 redibly strong repulsion that nor-
 ceeps nuclei at atom's length.

over, muons seemed to promise a
 able chain reaction because they
 be kicked out as fusion occurred
 uld thus trigger additional reac-
 By the mid-1950s, though, that
 petered out because the muon
 extremely brief life span—two
 hs of a second—before it decays
 aller subatomic particles. Physi-
 alculated that for cold fusion to
 muons would have to last much
 than that. But in 1977 new re-
 indicated that muons could do the
 aster than previously thought,
 racking the door to cold fusion.

ES HAPPEN. Since then a small
 d by physicist Steven E. Jones at
 n Young University has been
 g away in relative obscurity on
 ing budgets. Scientists familiar
 is work tend to be more im-
 by the Fleischmann-Pons revela-
 miracles happen," says Hendrik J.
 orst, a physics professor at the
 city of Florida. Researchers work-
 conventional fusion, he says,
 't been able to break the repul-
 urrier because they didn't think
 ough."

nd 1985, Jones and his collabora-
 dozen or so researchers in the
 nd Europe—branched out to ex-
 ther avenues. Because muons can
 e produced in very expensive
 nashers, Jones decided to look
 her alternatives, including cram-
 euterium ions into the crystal ma-
 metals. "The work was promising
 ense that it identified a new way
 ting nuclear fusion, even though
 was no strong indication that it
 be practical," says Ryszard Ga-
 director of the Energy Dept.'s
 of advanced projects, which has
 nding Jones's research.

1 Pons and Fleischmann began
 g their own experiment in late
 st down the road from BYU, it
 vitable that the two teams would
 out each other. A competitive ca-
 rie developed, culminating in a
 agreement that both groups
 submit progress reports to run in
 e issue of *Nature*.

University of Utah's press confer-
 ught the Jones team by surprise.
 mbers have been biting their
 s for fear that premature publici-
 cause *Nature* to reject their pa-
 t from what little Jones and his
 are saying, it's clear that they
 so detected fusion within metal

crystals—though the energy outflow is
 much smaller than that reported by
 Pons and Fleischmann. The Jones team
 has "checked and double-checked" its re-
 sults at several labs, says one collabora-
 tor who asked not to be named.

What perplexes most scientists is the
 claim by Pons and Fleischmann that
 their device produced four watts of heat
 energy for each watt of input during
 several experiments that lasted for 100
 hours or more. "If I know anything
 about physics, [those results] are
 wrong," declares Robert L. McCrory, di-
 rector of the University of Rochester's
 Laboratory for Laser Energetics. Get-
 ting that much heat, says McCrory,
 would require the emission of "a trillion
 neutrons per second—and in one hour
 they'd have a lethal dose."

That may be true for high-tempera-
 ture fusion, says Michael Danos, a physi-
 cist at the National Institute of Stan-
 dards & Technology, but the calculation
 doesn't hold once the deuterium ions are
 stuffed into a crystal. In that case the
 esoteric forces of quantum physics com-
 plicate matters. Every so often a deute-

rium nucleus will make a quantum jump
 and "tunnel" through the repulsive bar-
 rier. The chance of that happening is
 only 1 in 10 billion or more, but Jones's
 research reportedly shows that by se-
 lecting a crystal that forces the ions into
 closer proximity, the odds improve sig-
 nificantly. A mixture of deuterium and
 tritium, a hydrogen isotope used in hy-
 drogen bombs, speeds up the process
 even more.

But two key questions remain: Can
 crystal-catalyzed fusion happen rapidly
 enough to be an efficient source of ener-
 gy, and can the process be scaled up to
 commercial size? Fleischmann and Pons
 are confident that it can, perhaps by
 soon after the turn of the century. And
 the Energy Dept. is certainly impressed:
 It's funding their next 18 months of
 work, to the tune of \$322,000.

Few others are so baldly optimistic.
 "If they're right, it will solve a lot of the
 world's problems," says Park of the Uni-
 versity of Maryland. "But I wouldn't
 mortgage the house on it."

*By Otis Port in New York, with John
 Carey in Washington and bureau reports*

BIG SCIENCE'S FUSION RACE IS STILL AT A CRAWL

For 40 years scien-
 tists have sought to
 harness the sun's
 fusion furnace for plenti-
 ful power on earth. But
 after an estimated \$20
 billion in research, com-
 mercial fusion power still
 remains decades away.
 The hurdle: the engineer-
 ing difficulties and high
 price tag. "You crawl to
 success in the fusion
 business," says Robert L.
 McCrory, director of the
 University of Rochester's Laboratory
 for Laser Energetics.

Until the recent advent of "cold fu-
 sion," physicists have been using two
 main techniques to build fusion reac-
 tors. One involves heating up an iso-
 tope of hydrogen called deuterium to
 millions of degrees. At those tempera-
 tures, the fuel is so hot that it would
 burn through any known material. So
 scientists in the U.S., Soviet Union,
 Europe, and Japan have constructed
 expensive doughnut-shaped machines,
 known as tokamaks, which bottle the
 fuel in powerful magnetic fields.

In a milestone experiment last fall,
 the tokamak reactor at Princeton Uni-
 versity reached a record temperature
 of 300,000,000F. Still, the experiment



PRINCETON TEST REACTOR

consumed more than twice
 as much energy as it pro-
 duced. "Now we're not
 that far away from break-
 even," says Harold P.
 Furth, director of Prince-
 ton's Plasma Physics Lab,
 referring to the point at
 which the reactor will pro-
 duce as much power as
 it uses to maintain the
 reaction.

MORE POWER. In the rival
 approach, called inertial
 fusion, scientists smash
 tiny glass bubbles of deuterium fuel
 with a powerful laser. At Lawrence
 Livermore National Laboratory and
 the University of Rochester, physicists
 are boosting their lasers' power in a
 race to achieve the "breakeven" goal.

But the federal budget crunch is
 slowing the fusion race. The Energy
 Dept. is spending \$350 million this year
 for magnetic fusion and another \$164
 million for laser programs. That's not
 nearly enough to fund scheduled ex-
 periments. Princeton, for example, had
 hoped to begin building a new tokamak
 reactor in 1990, but has put the plan on
 hold until at least 1994. The University
 of Rochester is still waiting for fund-
 ing for designing and building a more
 powerful laser.



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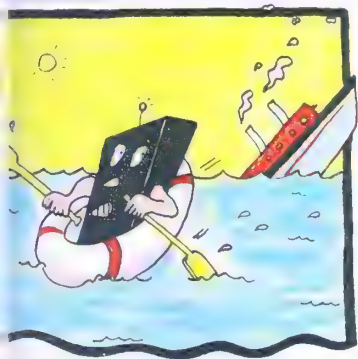
**OFFICE
ACCESS**

*The way to become well-connected
in the business world*

Developments to Watch

BY EMILY T. SMITH

A SHIP'S SECRETS IT'S NOT SINK WITHOUT A TRACE



Every airliner has a flight recorder that automatically logs a plane's performance and instrument readings. This "black box" is the first thing that investigators search for after an accident. Now, Lloyd's Register of Shipping has come up with one for ships.

"float recorder" relies on sensors and miles of wires to crucial data: a ship's speed and direction, whether watertight doors are open or closed, the degree of pitching and the strain on the hull. The system also monitors weather conditions including wave height and wind velocity. If the ship sinks or the black box is threatened by fire, the device is automatically activated and sends out a radio location signal. The device's recorder, which costs more than \$115,000, will help determine the cause of maritime accidents, many of which are never explained because ships still go down without a trace. The device can also be used during a voyage to provide clues on how to shift cargo during a storm to avoid undue stress on the hull. The first customer is London's International Marine Services Ltd., which will fit the device on its 27,000-ton container ship, Gulf Spirit.

LE-YOU-WAIT BLOOD TESTS OUR CORNER DRUGSTORE

For many Americans, the local drugstore is a refuge of first resort for aches, pains, and illnesses. Now, thanks to technology, there may be new reasons to stop by the pharmacy. In a new program, drug distributor McKesson Corp. will launch a program of 14,000 independent pharmacy customers are already signing up for in-store cholesterol screening.

Using a portable chemical blood analyzer made by Abbott Laboratories, nurses simply prick a customer's fingertip and get the results within eight minutes. The attraction for consumers is clear: The test will cost just \$7, compared with a minimum of about \$35 in most medical facilities. But that's just the start. The machines can run a gamut of blood chemistry tests from glucose testing, which can signal diabetes, to triglyceride levels, a sign of cardiovascular health. Managers of independent laboratories that customarily charge big markups on tests may soon be clutching their chests.

BERT MURDOCH'S SCHEME TO CUTTLE VIDEO PIRATES

Television—the new satellite-based TV service launched in Britain in February by media mogul Rupert Murdoch—is drawing a hard line against video pirates. To frustrate would-be thieves, who plague U.S. pay-TV operators by tuning in illegal black-box decoders, Sky TV will change its decoding method every three months. That way most buccannons won't have time to figure out the scheme and get

decoders on the underground market before the codes are changed again.

Legitimate viewers will "unlock" the Sky Movies and Disney Channel signals with a decoder activated by a so-called smart card—a credit-card-size slab of plastic with a microchip buried inside. Subscribers will get a new card every three months. If a viewer doesn't ante up \$50 for the next chip card, even an authorized decoding box won't work. The encryption scheme was developed by Adi Shamir, a professor at Israel's Weizmann Institute of Science and a founder of News Datacom Research Ltd. in Jerusalem, which markets the technology.

A NEW CONTRACEPTIVE THAT MAY ANTIQUATE THE PILL

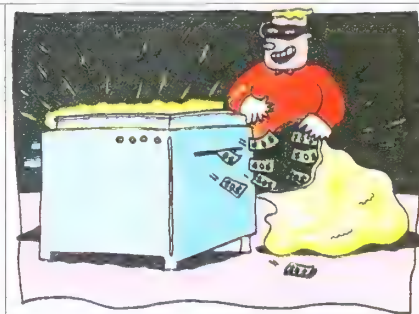
Birth control pills are among the most effective forms of contraception, but many women don't use them because they can cause side effects. Now a contraceptive ring that is placed inside the vagina is proving to be even more effective than pills, with fewer side effects. The Dutch maker of the device, Organon International, says 90% of women who used the ring prefer it to other methods of contraception. And in a major test, none of the women became pregnant.

The flexible silicon-rubber ring is left in place for three weeks, gradually releasing tiny amounts of the two hormones normally found in oral contraceptives, progesterone and estrogen. The ring is then removed for one week, just as women on the pill stop taking tablets, and bleeding resembling a period occurs. One ring is effective for four months.

An obvious advantage of the ring is that women do not have to remember to take a pill every day. And lower doses of the hormones can be used because they are absorbed directly into the body at a regular rate through the vaginal wall. That means that large amounts of the hormones do not pass through the liver, as with orally ingested pills. So major side effects, such as blood clots and increased risk of heart disease, are reduced.

THE LASER COPIER GIVING G-MEN THE CREEPS

Making counterfeit money used to be an art, but photocopying is the name of the game these days. In fact, Canon Inc.'s high-end laser copiers are so good at churning out bogus currency that even experts have a rough time telling the copies



from the real McCoy. That's why the Royal Canadian Mounted Police keep a record of every buyer of the Canon color copier.

José Martins, 30, a community-college dropout in Ste. Catherine's, Ont., recently wrote a check for \$25,000 (Canadian) as half-payment on such a machine. Then he ran off more than \$24,000 in U.S. and Canadian bills. Before Martins passed any of his notes, his check bounced, and the copier was repossessed. Beneath the cover were a couple of new bills, which the retailer reported to the RCMP. Martins was convicted.

The U.S. Treasury Dept. worries about "lunch-time counterfeiters"—ordinarily honest folk who will treat themselves to a "free" lunch. To help detect bogus bills, the Treasury will add special threads to its paper. Canada is considering holographs.

A&P IS THRIVING—SO WHY IS JAMES WOOD STILL AROUND?

This time, the turnaround ace is settling in for the long haul

Like most visitors to New York, James Wood tries to get the most out of every trip. Not long ago, the chairman of Great Atlantic & Pacific Tea Co. made the hour's drive to the city from his headquarters in Montvale, N.J., to spend the morning with securities analysts. Next on his agenda was a little sightseeing: He was going to pay surprise visits to each of his Manhattan stores. But first Wood needed lunch. Windows on the World? The Four Seasons? Try McDonald's.

Wood, 59, can certainly afford something better than a Big Mac. But he's a man in a hurry. Since 1980, when he bitterly walked away from his job as a turnaround specialist for British financier Sir James Goldsmith, he has transformed the once-ailing A&P into one of the nation's strongest supermarket chains. Massive store closings, strategic acquisitions, skillful bargaining tactics, and strict cost controls have helped boost profits to \$127 million in 1988, from a net loss of \$43 million in 1980. Revenues during that period climbed from \$7 billion to \$10 billion. And because of bonuses tied to A&P's stock, which has soared from 4 to around 48 under his guidance, he has personally made more than \$70 million.

RE-UPPING. Now Wood, an Englishman, is doing something he has never done in a turnaround: He's staying put. With his 10-year contract set to expire in 1990, he recently signed on for another five years. A&P will probably never regain the power it had in the 1930s, when its 15,000 stores dominated the grocery business, but Wood thinks there's plenty of room for more growth. "This is more than just a turnaround," he says. The German Tengelmann Group, which owns 52% of A&P, couldn't be happier (box).

Yet the next five years may be Wood's toughest. The cornerstone of

A&P's growth strategy has been acquisitions. But after several years of frenzied buying in the industry, the company may be hard put to find more grocery chains at decent prices. In the South,



A LA CARTE: WOOD SAYS THERE'S NO DEARTH OF CHAINS TO BUY

where A&P's profits and margins have dragged, Wood tried to acquire Delchamps Inc., a chain based in Mobile, Ala., but the family-owned company rebuffed him three times. A&P also tried and failed to buy several New England supermarket groups.

Another potential problem: A&P's heady growth may slow down once its overhaul is complete. Since taking over, Wood has built 220 stores, expanded or remodeled 400, acquired 475, and shut

down nearly a thousand. But after the deadwood has been cleared out about 1990, it may be tougher to do the 20% annual profit growth that has promised to investors.

Nonsense, says Wood, arguing that wouldn't have signed on for five years if he weren't sure he could get things moving quickly. He claims there's no dearth of acquisition targets. Independent chains that may have been too small five years ago are ripe for plucking, he says.

FUTURE STOCK. Wood contends that without new acquisitions he can promote growth by continuing to change the mix of products his stores sell and by experimenting with new formats. To capture upscale customers, A&P has opened 29 "future stores" which feature high-margin items such as seafood, flowers, and hot take-out food. In New York, the company's 17 Emporiums have operating margins of 4% vs. A&P's overall margin of 2.7%. Wood is beginning to export the format to other cities. A&P has also been pushing its own high-margin line of coffees and jams, under the "Master Choice" label.

Many of Wood's merchanting changes, such as the move toward high-margin items, mirror trends in his industry. But he's not usually one to run the pack. Associates describe him as a loner. At industry conferences, he often walks out of meetings early, and he rarely joins peers for cocktails or a sip. But Wood can be disarmingly charming, with an engaging manner and a disarming smile. And he knows it's the little things that count. At his first meeting with the management of Waldbaum's, after taking over the chain in 1986, he put the company's Jewish founders at ease by serving bagels and lox. Wood also led a high-profile effort to sell Israeli bonds, a move that acknowledges may have helped him acquire both Waldbaum's and Borman's, also owned by a Jewish family.

If Wood makes the supermarket business look easy, it's probably because he has been in it for 45 years. The son of a building contractor, he grew up in Newcastle-upon-Tyne, and at 14 he became a grocer's apprentice. Wood joined Goldsmith in 1965, at 35, answering an advertisement in *Financial Times* ad for a director. He helped the financier

round, and sell a dozen retailers several real estate properties.

By 1980, Wood was becoming restless. For six years he had been running A&P's Grand Union chain in the Midwest. But Goldsmith's promise of an equity stake in the parent company materialized, Wood says.

Wood declined to comment. Nevertheless, when Tenenbaum owner Erivan Haub offered Wood the top job at A&P last year, his impatience with Goldsmith made him jump. "The German billionaire said, no way in the world would I be interested in another one of these guys who wants you to do a deal for him," Wood recalled. But Haub wisely offered what Goldsmith didn't: the promise of 10% of Haub's stake in A&P.

RIGHT AIM. Wood did not want to think the offer over for long. "I stayed up in bed smoking cigars all night," he said. "The next morning, I called Jimmy in London and said: 'Now who you're talking to? The man of A&P.'" Wood says the two are friends, but jokes: "I don't know

how long Wood prides himself on his negotiating skills, colleagues say he's excited by doing deals. In the past years he has spent about \$600 mil-

lion acquiring regional chains with strong merchandising profiles in markets where A&P already had a strong presence. The company now owns about 1,250 stores, down from 1,600 in 1980.



WOOD'S SHOPPING SPREE

Year	Acquisition	Region	Price Millions	A&P's market share
1983	KOHL'S FOOD STORES	Milwaukee	\$31	24%
1985	DOMINION STORES	Ontario	116	20
1986	SHOPWELL*	New York	70	29
1986	WALDBAUM	New York	277	29
1989	BORMAN'S	Detroit	76	34

*Includes Food Emporium

DATA: MACLEAN HUNTER MEDIA INC. AND COMPANY REPORTS

Combining operations cuts costs, and in New York and Detroit has made A&P the market leader. In cities like Milwaukee, where he felt the A&P name had been hopelessly tarnished by years of neglect, Wood also renamed all the A&Ps after newly acquired chains.

He has also brought financial discipline to the often poorly run family operations he has acquired. Says Aaron Malinsky, president of Waldbaum's: "He taught us to clean the gun and aim it straight." Wood has a way of making

labor do things his way, too. In Philadelphia, when Wood failed to win concessions from union workers in 1981, he shuttered all 80 stores there. Ten months later workers agreed to major concessions in exchange for a progressive incentive plan: Workers get bonuses if they can keep labor expenses below the industry average.

Sometimes Wood's "progressive" ideas border on science fiction. He dreams of a day when city supermarkets will be nothing but aisles of computer screens, with the food delivered direct from warehouses to customers' doors. But for now, Wood has more immediate concerns. First he has to find a replacement for his former heir apparent, Louis Sherwood, who left when Wood announced he was staying on. More important, he must find a way to keep A&P growing. He has plenty of reason to do so: For every point A&P's stock rises, he stands to make \$1.8 million in bonuses from Haub. That works out to more than a million Big Macs per point.

By Andrea Rothman in Montvale, N.J.

HOW A GERMAN SUPERGROCER GOBBLED UP A WINNER

Billionaire Erivan Haub, sole owner of West Germany's Tengelmann Group, was traveling in New York when he heard the news: Atlantic & Pacific Tea Co.'s ruling family wanted to sell its hold- ing in the once-mighty A&P supermarket chain. Inspired by the idea of re- tating a dying giant, Haub quickly red 50% of its stock for about million. Only later, friends say, Haub learn how much help A&P needed.

A decade later, after several rough years, Haub's risky investment is pay- ing off handsomely. His original stake in A&P, which he has since upped to 50%, is worth roughly seven times what he paid. And A&P now accounts for more than half of Tengelmann's sales. A&P reported 1988 sales of \$1.1 billion, compared with about \$8 billion for the Tengelmann chains in Ger- many, Austria, and the Netherlands.

Haub, 57, is an intensely private man. Even in Germany, where he em-

plloys more than 50,000 workers at his Tengelmann, Kaiser's, and Plus stores, he avoids public appearances and isn't well-known by his countrymen. But his Tengelmann Group is known to many. Founded 121 years ago by Haub's great-grandfather, it is West Germa-



TENGELMANN'S HAUB: SHOPPING IN THE U.S.

ny's largest private retailer. With around 4,000 stores, it is Europe's big- gest supermarket chain.

Not surprisingly, Haub has spent his whole career in the grocery business—but not all of it in Germany. After

studying economics at the University of Hamburg, he worked for three years at Jewel-T stores in Illinois and the Alpha Beta chain in California. Haub still feels a strong attachment to the U.S.: He arranged for his three sons to be born in America so they could be citizens. Haub and his family own a summer home in Tacoma, Wash.

Some Wall Street analysts speculate that Haub might either take the A&P chain private or cash in his stock. But he denies both possibilities. In fact, because antitrust laws in Germany limit the number of acquisitions he can make there, Haub is likely to hang on to A&P as a tool for expansion in the U.S. Perhaps as a sign of pride in his American supermarket, Haub even sells the A&P brand in his European stores. But over there, the letters don't stand for Atlantic and Pacific. They're short for "attraktiv und preiswert"—attractive and bargain-priced. Just like his A&P investment.

By Andrea Rothman in New York

PAN AM NEEDS A PARTNER, BUT DOES ANYBODY NEED PAN AM?

Its aging fleet and high debt may put off other carriers

The strike at Eastern Air Lines Inc. has handed Pan Am Corp. a golden opportunity on the Northeast corridor. While Donald Trump and Frank Lorenzo publicly squabble about the sale price of the Eastern shuttle and Eastern struggles with its bankruptcy, Pan Am executives are busy deploying widebodies to accommodate the surge in demand for their own shuttle service. Pan Am now commands an estimated 85% of the shuttle market.

But the success of the three-year-old Pan Am shuttle can barely begin to repair the damage of a decade of failure at the parent company. And Pan Am suffered a major blow in the tragic explosion of Flight 103. The terrorist act has obviously hurt business: Traffic on Pan Am's transatlantic routes was down 15% in January and 20% in February. And the fears persist: Just before Easter, IBM advised its employees in Europe and the Midwest to avoid flying U.S. carriers from those areas until the end of April.

Pan Am's deterioration predates Flight 103 by years. Long-term debt is almost \$870 million. The unfunded pension liability is \$535 million. And even though many of its 747s have been refurbished, Pan Am operates one of the oldest fleets in the business. The carrier has firm orders for just two planes. And in Europe, Pan Am's lucrative system of routes between West German cities and Berlin now faces stiff competition from Luft-hansa and Air France.

In February, Chairman Thomas G. Plaskett publicly admitted the obvious. He said that Pan Am must team up with

another carrier. Plaskett's candor helped drive the stock up 30%, to more than 4.

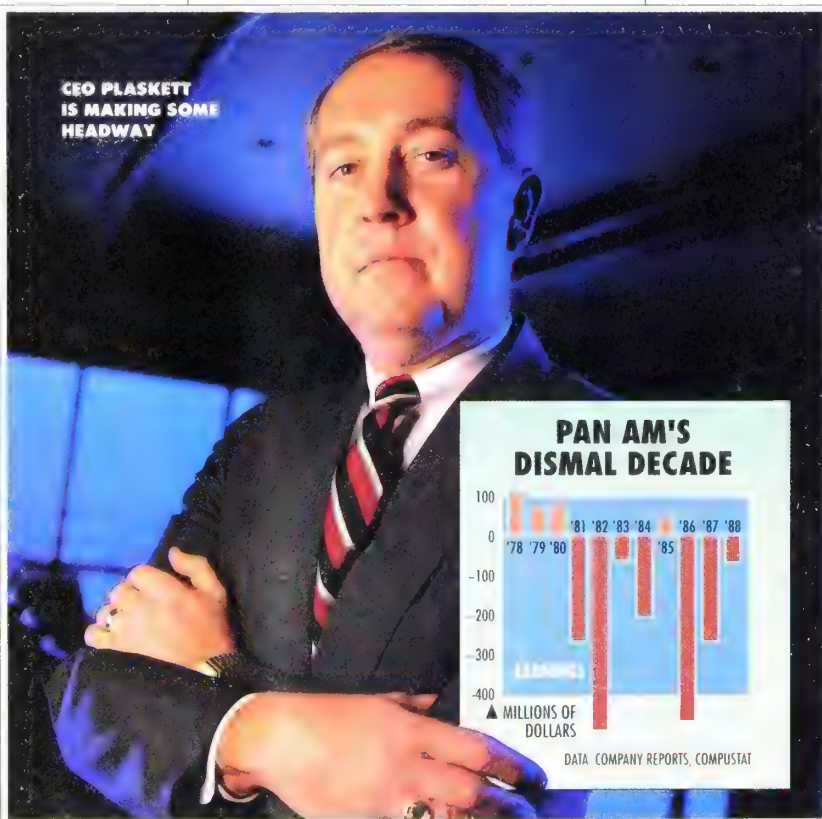
Plaskett's announcement was the latest move in his efforts to give the ailing carrier a viable future. Since January, 1988, Plaskett has cut back on the number of Pan Am tickets available to wholesalers, who sell at a discount and reduce an airline's profits. He has ex-

1988 losses narrowed to \$73 million, sales of \$3.6 billion. If the threat of terrorism abates, summer travel is strong and Eastern remains a weak competitor. Pan Am could approach the breakeven point this year.

'PRETTY DICEY.' But Plaskett knows doing less is not the way for Pan Am to replace its fleet, improve its service,

compete with heavyweights such as Delta, American, and United, which use big domestic networks to channel passengers to their growing system of overseas routes. "The megacarryers control the industry," says Plaskett. "It makes expansion on our own pretty difficult."

A deal with an outside investor—a new Pan Am's unions proposed long before Plaskett arrived—might provide a lifeline. To attract a partner, Pan Am has launched a shuttle, a money-losing commuter airline, a generally prosperous South American system, and valuable routes and gates at congested airports such as London's Heathrow. There's also Pan Am's value as a brand name. "The Pan



panded a frequent-flier program for executives. By selling off orders and options for Airbus aircraft, Plaskett has also piled up about \$300 million in cash, which Pan Am needed to carry it through the slow winter season. Moreover, Plaskett has extracted \$170 million in pay cuts and work-rule changes from the flight attendants, pilots, and mechanics. Pan Am's Teamsters, however, still work without a contract: A Teamster strike is possible but unlikely.

Thanks to these efforts and some strong business last year, Pan Am's

name is still incredibly respected overseas," says Matthew Scocozza, a transportation lawyer and former Assistant Secretary at the Transportation Department.

A strong U.S. airline could make use of the Pan Am name, through either outright acquisition or an alliance that involved a hefty dose of capital. Plaskett says another option is for Pan Am to buy another property, an outcome that seems unlikely considering the carrier's anemic balance sheet. Nevertheless, Plaskett would consider buying Eastern's assets, such as its hub in San Juan.



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Puerto Rico, if they went up for sale. Nobody, however, has yet beaten a path to Pan Am's door. United Airlines Inc. has stated publicly that it has no designs on Pan Am. American Airlines Inc. might like part of Pan Am, but Plaskett swears he will not sell the airline operations piecemeal.

Plaskett may have hurt his chances for a good deal by appearing to be in too much of a hurry. "It surprised me he made his move so soon," says Raymond E. Neidl, an airline bond analyst for McCarthy, Crisanti & Maffei Inc. "You would think he would have waited until he had made Pan Am a viable entity."

It may be that Pan Am, after selling its Pacific division and its hotels years ago, does not have enough to offer, given its high debt and old fleet. "I just don't see anybody running to Pan Am," says the chief executive of a major airline. "It's a tired system."

If Pan Am did manage to attract the attention of a major U.S. airline, others might bid, however reluctantly. "Some airlines don't want to get involved with Pan Am, but they don't want anyone else to, either," notes Robert Joedicke, an advisory director and airline specialist at Shearson Lehman Hutton Inc.

JAPANESE HELP. Another possibility is a foreign alliance. Pan Am, though a minor-league player domestically, does fly to many airports around the country. That access might appeal to some foreign carriers, which cannot fly passengers within the U.S. And Pan Am has valuable routes to the Caribbean and beyond. "Pan Am's network is less extensive than others," says Ken Kato, manager of Japan Air Lines Co.'s international passenger division. "But it's still attractive to JAL, which has lots of passengers headed for Latin America." Kato says JAL has no specific plans for Pan Am, but he does say closer ties are worth considering.

If no U.S. or foreign carrier emerges as a partner, Pan Am will have to struggle on alone. It certainly has enough cash to survive another year, but without substantial new capital, Pan Am would continue to weaken. An economic slowdown could drain away even more of its resources. "Tom Plaskett gets the red badge of courage for taking this job on," says Daniel M. Kasper, a transportation specialist at Harbridge House, a consulting firm in Boston.

Plaskett seems to be doing everything he can to save Pan Am. But he needs allies, money, and luck—advantages that this venerable airline has vainly sought for many years.

By Christopher Power in New York, with Ted Holden in Tokyo and Seth Payne in Washington

STRATEGIES



CEO GEORGES SALOMON: HIS WORLDWIDE RETAIL NETWORK IS ITCHING FOR NEW PRODUCTS

THE SLOPES ARE GROOMED FOR SALOMON'S NEW SKI

He expands from boots and bindings to rival the top ski makers

Georges Salomon doesn't spend much time behind a desk. The more mundane aspects of running Salomon, the French-based ski-equipment maker, bore him. Look instead in the product-development lab. There, clomping around in ski boots and a baggy sweater, the 62-year-old chairman does what he likes best—devise ways to frustrate his competition.

Starting out with the patent for metal ski edges his father registered in 1947, Salomon has built one of the world's largest winter-sports companies, with sales of \$467 million. In 1972 he schussed past Austrian-based Tyrolia to become the leading maker of ski bindings. With a rear-entry ski boot he introduced a decade ago, he is pressing Italy's Nordica for the No. 1 spot in boots. Now, Salomon plans to enter the ski business with a product he calls "revolutionary." His goal: a 20% slice of the market.

FEUDING. But Salomon may hit some moguls. Market saturation and snowless winters have slowed industry growth to 2% annually for the past four years. So, Salomon's ski will have to win market share to prosper. While much of the competition is fragmented and pinched financially, he will get a battle from French archrival Rossignol, the industry leader with 26% of the \$830 million global alpine-ski market. Rossignol, with sales of \$256 million, has entered the boot business, vowing to fight Salomon across the board.

Both companies hope broader product

lines will help them grow. "You won't win in this industry if you stay small," says Rossignol Chairman Laurent Boix-Vives. Once close friends who traded technical information and staged joint advertising programs, Salomon and Boix-Vives are now feuding. Boix-Vives claims Salomon enlarged his stable of ski engineers and that he once swiped a Rossignol boot from a trade show. Salomon, who pooh-poohs the charges, says Boix-Vives' gripe is sour grapes.

Industry oddsmakers give Salomon the edge. While rivals dismiss as hype Salomon's claim that his ski is revolutionary, they have no doubt it will be briskly when introduced next winter. "What I'm worried about is their sales and distribution clout," admits Jan Garrison, president of U.S. ski maker K2 Corp. Salomon's success in boot and binding has its worldwide retail network itching for a new product. Salomon is well placed to keep up the heat. While an ailing tennis racket culture and high marketing costs cut Rossignol's earnings 29.4% for the year ending Mar. 31, Salomon's purchase of Chicago-based Taylor Golf Co. has been a great success. Booming sales of the unit's clubs helped raise profits 13.9%, to about \$10 million this year.

Salomon's tinkering has paid off handsomely. Whether or not his new ski will be fast enough to catch Rossignol remains to be seen. But for now, the momentum is his.

By Ellen Wallace in Annecy, France

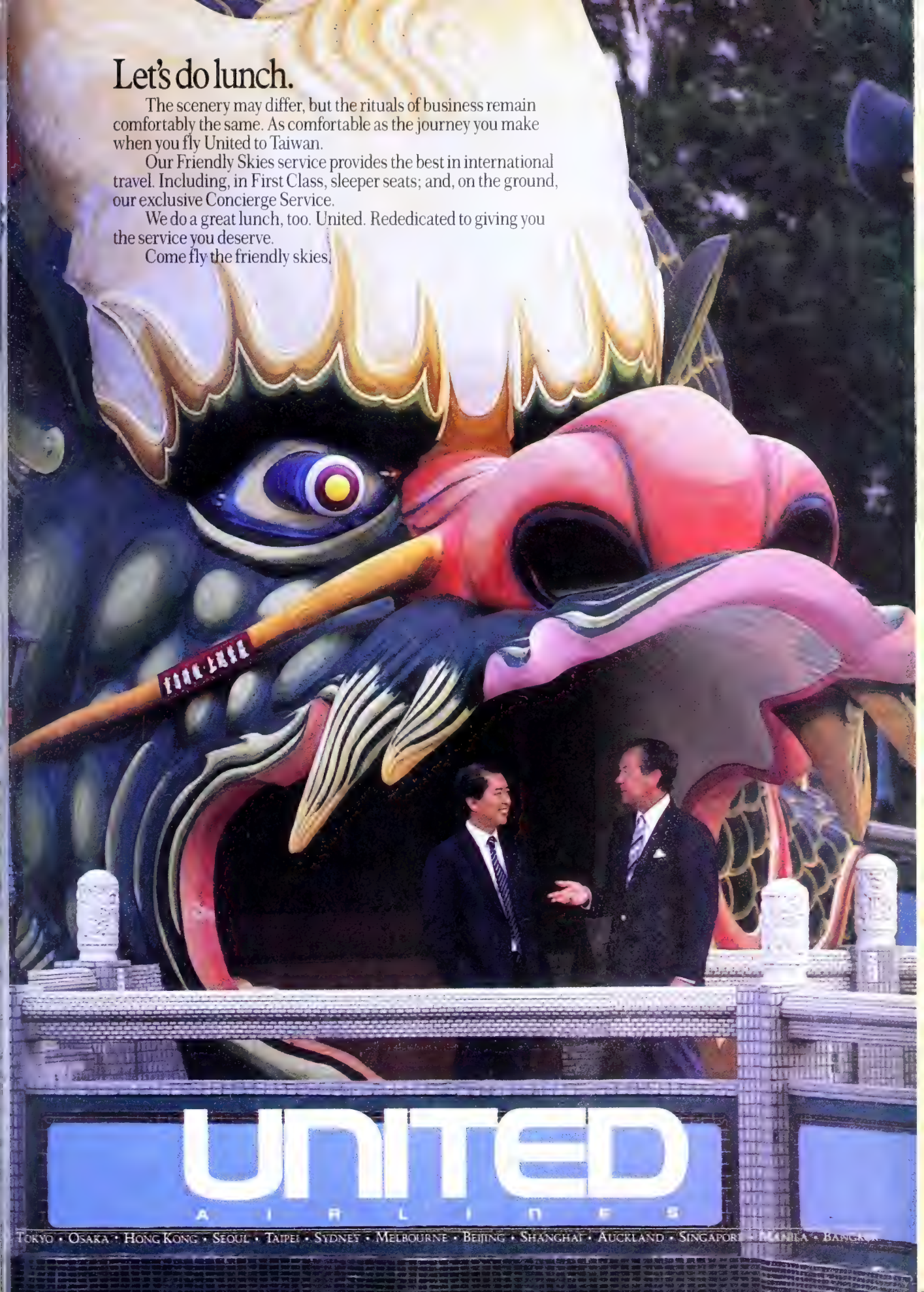
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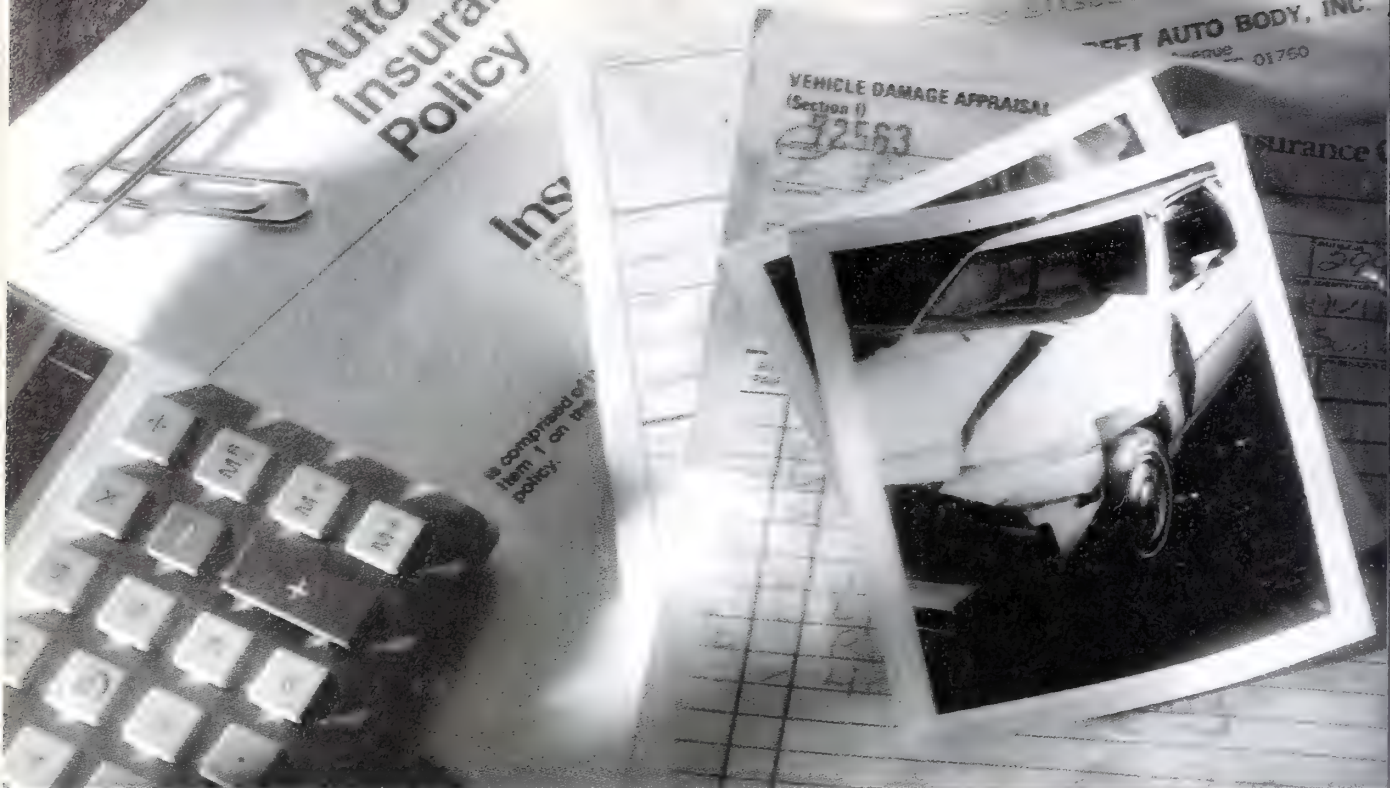
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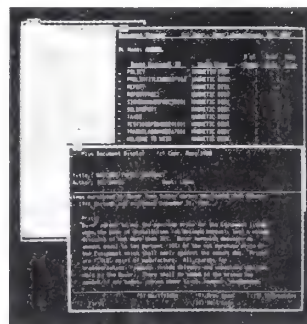
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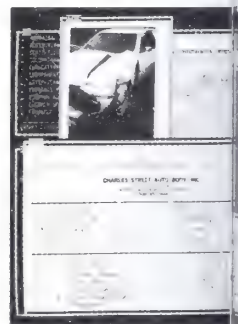
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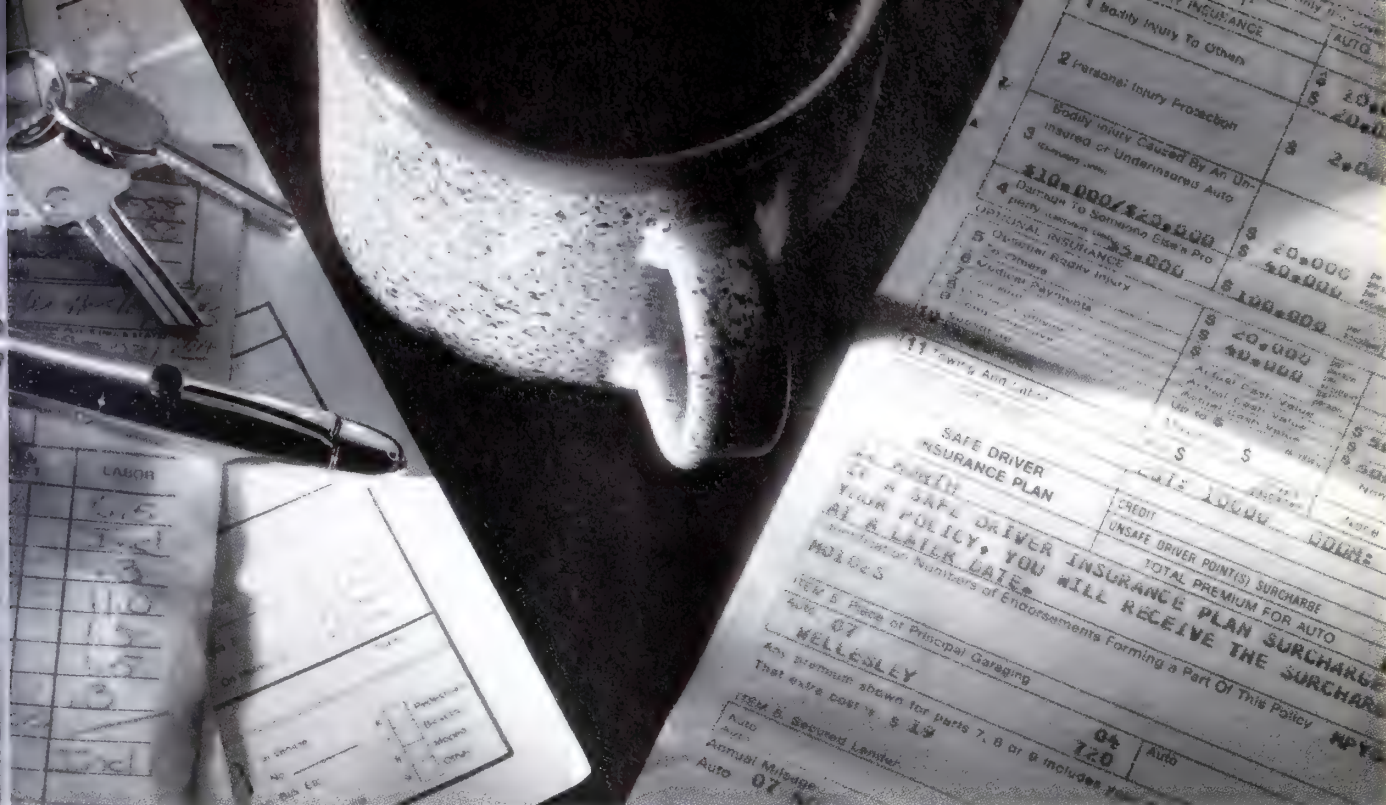
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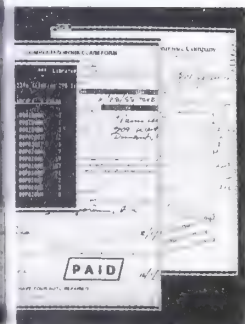
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ALARM SYSTEMS THAT PAY OFF IN PEACE OF MIND

It used to be that all you needed to feel safe in your home was a good lock on the front door. But these days people are going to far greater lengths to keep intruders out—or detect them if they manage to break in.

If a surge in crime in your area has you thinking about buying a burglar alarm, you're in good company. The \$5 billion-a-year home security industry has been growing at an annual rate of 15%. And the good news is that burglar alarms are not only becoming more sophisticated and easier to use but less costly, too.

The average price of a professionally installed alarm system has fallen 50% since 1979, to \$1,500. And do-it-yourself systems, which use the same technology as the pro models, can be had for around \$400, with some basic systems selling for as little as \$139. A real bonus: In most states you get a 5%-to-10% discount on your homeowners' insurance.

NO 'CLEAVERS.' Of course, there's a bigger consideration than price. With the preponderance of two-career families, even cozy suburban neighborhoods have become virtual ghost towns from 9 to 5. That makes them easy targets for burglars, whom police say now do most of their business during daylight hours. Frequent overnight business trips and less contact with neighbors make today's homeowners even more vulnerable. "Today you don't have any June Cleavers looking out the kitchen window," says Robert Guzikowski, product manager for Schlage's Keepsafer home security system.

The alarms are effective deterrents. According to the FBI,

homes equipped with centrally monitored alarm systems are 15 times less likely to have a break-in. Most of the time, an experienced burglar realizes you have an alarm—either from seeing a sticker on your door or noticing sensors on the windows—and will go down the street instead. Nationally, just 7% of homes have alarms. "A burglar is like a lion in the jungle looking for the weak antelope," says Howard Parrott, an officer with the crime prevention unit of the Houston Police Dept.

Choosing a system takes some thought. The industry has a plethora of products ranging from simple but effective magnetic sensors that sound an alarm when a door or window is opened to devices that detect intruders by monitoring sound, temperature, and air movement. One system, the Dicon 9000 (\$600), has a voice synthesizer that will "talk" you through the installation process and then alert you whenever the system needs attention. If a break-in occurs, it will also tell you which door or window was tampered with. Other sophisticated systems will even adjust your lights, switch on your stereo, and turn on the air-conditioning by telephone, giving your house that lived-in look while you're away.

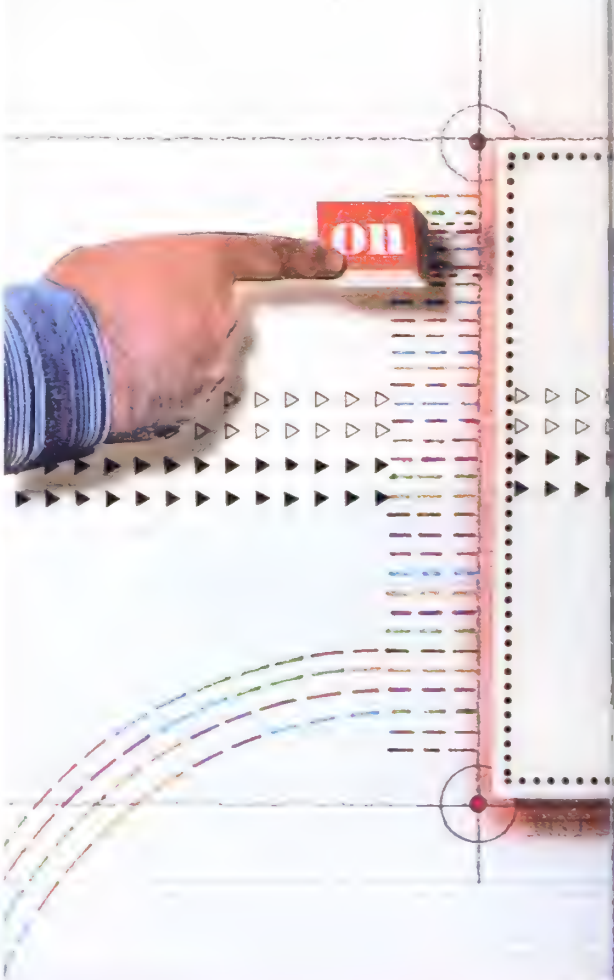
The first decision is whether to go with a traditional "hardwired" system or a wireless one. The latter uses radio frequency (RF) to communicate between the sensors on doors and windows and the controller, the brain of the system, which triggers the alarm. Hardwired systems are more labor-intensive to install. The technician has to run wires through your floor,

ceiling, and attic and attach them directly to the sensors and control panel. If the system malfunctions, it is more complex to repair. Still, hardwiring is the choice of most alarm companies because of their many years of experience with it.

PANIC BUTTON. Wireless systems, which first appeared about 10 years ago, have been refined to the point where they rival hardwired systems for reliability. Early wireless systems did have problems. Some could be triggered by remote-control devices, such

as automatic garage openers, which also operate via RF signals. Most newer wireless burglar alarms use digitally encoded frequencies that prevent overlap with other household appliances using RF. Black & Decker, for instance, uses a non-RF audio signal.

Wireless systems are much simpler to install. In most, they require only a couple of screw holes on a door and window you want to protect. Most products offer toll-free telephone help, and one even comes with



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FOUR HOME SECURITY SYSTEMS

System	Price	Features	Disadvantages
DIMANGO SAFE & SOUND	\$139	Wireless; 2 sensors, indoor siren; 72-hr. battery backup; remote control	No central station monitoring
SCHLAGE KEEPSAFER	199	Wireless; 2 sensors, indoor siren; wide variety of options	Sirens are hardwired to controller and could be defeated
BLACK & DECKER HOME PROTECTOR	499	Wireless; 6 sensors; 24-hr. battery backup; lamp flasher	No panic button or smoke detector
ADT SECURITY SYSTEMS (for 2,500-sq.-ft. home)	2,000	Hardwired; professional installation required; includes sensors for doors, windows, motion, smoke, heat	Not portable

DATA: COMPANY REPORTS, BW

The object of the inside alarm is to unnerve the burglar and get him out of your house. Many systems are designed to flash interior lights as the alarm sounds. "What burglars fear most are noise and light," says Lucille Bur-

rascano, a detective with the crime prevention division of the New York City Police Dept. She also recommends that you attach a rooftop strobe or turret light to the alarm to help police find your house.

Second, although it will increase the cost of your system, police advise that homeowners put sensors on every door and window. Don't neglect the second floor; most people do, and burglars know it. And to keep the system activated during a power outage, invest in a battery backup good for at least 24 hours.

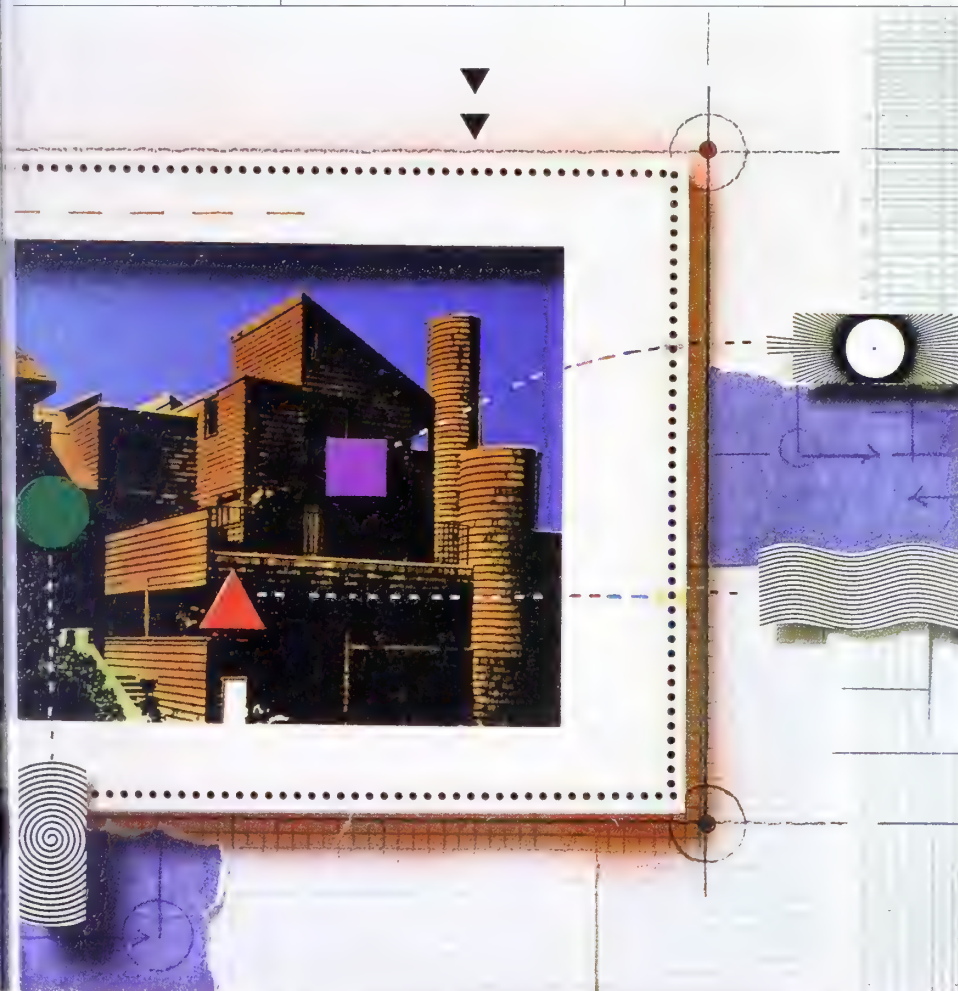
Furthermore, make sure your system has an exit-entry delay mode. It gives you up to 60 seconds to enter your house, lock the door behind you, and punch in your code before the alarm sounds. Remote-control devices that turn off the alarm before you unlock the door are popular, but police warn against them. Should a burglar rush in behind you, you'd have no way to sound the alarm.

FALSE ALARMS. Finally, because it's unlikely that police will be within hearing range of your alarm, you may want to contract with an alarm-monitoring service. For a fee averaging \$20 a month, the service—called a central station in the trade—accepts recorded phone messages from your automatic dialer. The dialer is attached to the system's controller and is activated by the alarm. The service calls you at work or another prearranged number and then notifies the police. Although automatic dialers can be programmed to call the police directly, police stations in most large cities refuse to accept such calls because they don't have the staff.

It's wise to check local alarm ordinances before installing a system. New York City requires that sirens turn off automatically within 15 minutes. Some cities, such as Houston, require a permit. If you don't have one, police responding to your alarm could fine you up to \$200. Also, check to see if you could be fined for false alarms.

Just because you have an alarm, don't ignore the basics of home security. No system will compensate for poor-quality locks on doors and windows. After all, the last thing you want to hear is that alarm.

Jo Ellen Davis



Smart Money

LOOK BEFORE YOU LAUGH AT 'CHAPTER 11' INVESTMENTS

Remember Interstate Stores, the discount retailer that went bankrupt in 1974? Four years later it emerged from Chapter 11 renamed Toys 'R' Us. Its stock soared, and early investors in bankrupt Interstate are now enjoying returns 50 times their original outlay.

Most bankruptcy stories don't turn out so well. While only 20% of publicly traded companies that file under Chapter 11 are liquidated, many emerge solvent yet still struggling. And in some cases, a bankrupt company's stock may skyrocket while its bonds remain battered—or vice-versa. But investing in bankruptcies can be enormously profitable if your timing is right (table). Returns can be especially high if, like A. H. Robins, Texaco, and Manville, the company files because of legal trouble, not to fend off creditors.

You may be tempted to buy during the month after a company files, when the stock is typically cheapest. The average stock loses 35% to 40% of its value in the month after the filing, and the typical bond loses about 20% of its value in the weeks after its default, says Professor Edward Altman of New York University's Stern School of Business.

But experts suggest you wait four to six months, then piggyback on the choices of institutional investors. The

pros usually take that long to decide whether a company is worth more in liquidation or as an ongoing concern.

It may be several years before you realize a profit. And if the company does get liquidated, common stockholders get paid back last—after banks, trade creditors, bondholders, and preferred stock holders.

TRACK RECORD. It's easy to spot a bankrupt company in the financial pages. Its shares have a VI next to them, and bonds no longer paying interest have an F. If you'd rather not invest in individual companies, there are several specialty mutual funds. Some, such as Mutual Series Fund in Short Hills, N. J. (201 912-2060), have excellent track records and require no minimum investment. Brokerages such as R. D. Smith (212 952-8100) have few restrictions. But others, such as Whitman, Heffernan & Rhein (212 888-5222) and Balfour Investors (212 489-7077), have entrance requirements that start at seven figures.

Roughly 16,000 companies filed under Chapter 11 in 1988, and hundreds of those that filed over the past few years were public companies. But for every A. H. Robins or Toys 'R' Us, there's a Storage Technology—no longer bankrupt, but its stock trades lower than before it filed. *Laura Zinn*

A SAMPLER OF BANKRUPTCY STOCKS

Company	Date entered*	Stock price month later	Date left*	Stock price 3/27/89
PUBLIC SERVICE OF NEW HAMPSHIRE	1/88	2 5/8	NA	4 1/8
TEXACO	4/87	37 3/4	4/88	53 1/8
A. H. ROBINS	8/85	7 3/8	NA	26 1/4
WHEELING-PITT. STEEL	4/85	8	NA	12 1/2
STORAGE TECHNOLOGY	10/84	3 1/8	7/87	2 1/8

* Chapter 11 reorganization proceedings NA = not applicable
DATA: BRIDGE INFORMATION SYSTEMS INC.



LOW-SLUNG, SWEET CHARIOT: THE 300ZX WILL GO FOR \$25,000

Autos

NISSAN'S NEW 'Z-CAR' GETS AN A FOR ACCELERATION

It was the thinking person's sports car—small, basic, and nimble. But since the Datsun 240Z hit the U.S. 20 years ago, Nissan's "Z-car" has grown heavy and plush, fit more for cruising boulevards than whipping through country roads.

That's about to change. A radically new 300ZX, as the "Z" is now called, is coming in late April. Designed to juice up weak sales at troubled Nissan, this two-seater will burn back roads with the best sports cars on the market.

ROAD-HUGGER. Don't expect a reincarnated 240Z, however. The college crowd that paid about \$3,700 for the first Z probably couldn't even afford the insurance on the new \$25,000 coupe. And the 1990-model Z is still a heavy car. At 3,200 pounds, it weighs 700 pounds more than its ancestor and even a few pounds more than last year's 300ZX. The car can feel ponderous, especially in city driving.

But if you like big, muscular sports cars with lots of comfort, it's hard to beat the 300ZX. It's a pretty car—wide, racy, and low-slung. Its supersmooth engine develops 222 horsepower, zooming to 60 mph in 7 seconds, a second less than last year's turbo Z.

On twisting roads, the Z makes last year's model feel like a family sedan. This one hugs the road like a race car with tight and predictable steering.

The new Z's interior marks its greatest leap forward. Last year's model had one of the auto world's most cluttered cockpits, jammed with gauges, chrome buttons and gearshift instrument displays. The 1990 is blissfully sober—round analog dials only.

The ride is extremely smooth. That's partly because of a longer wheelbase—though the body is four inches shorter than last year's. Seats are ultracomfortable, and the driver's seat adjusts in every conceivable direction. The stick shift has a short-throw lever.

Less admirable is the visibility. The rear window is nearly horizontal, so you see only a narrow slit through the rearview mirror. Side vision is blocked by thick pillars—partly the result of the Z's removable "T" top.

Despite its faults, the Z is a highly attractive car you had given up hope of. This legendary name will ever again grace a true sports car, take heart—the Z is back. *Stewart*

As Sarah's head broke through the water three inches from my eyes, she gazed into my eyes and smiled. I would have led, too, but I would have popped my snorkel. Ten minutes into my first "dolphin encounter," I had experienced a communion with one of nature's most fascinating creatures.

Dolphin "swim-withs" are a—and controversial—phenomenon. The programs provide a unique chance to gain insight into these intelligent mammals. But to environmental groups such as Greenpeace, there's a danger of exploitation. The worry is even that the National Marine Fisheries won't

allow any new programs until a study is completed and guidelines adopted in 1990. Meanwhile, there are four "swim-with" programs in Florida Keys. One at the Hyatt Regency Waikoloa. All cost \$40 to \$55 and require advance reservations, sometimes weeks ahead. But the programs vary greatly in philosophy and approach.

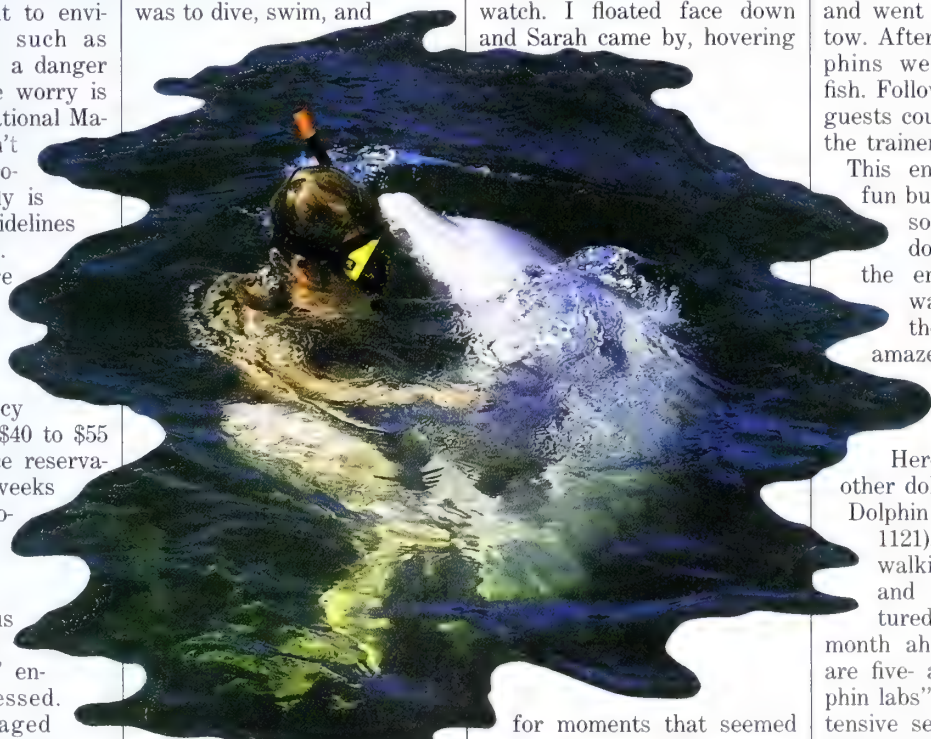
At Dolphins Plus in Key Largo (305 333-1993), "natural" encounters are stressed. There are no staged interactions or rewards, and a 40-minute orientation precedes the half-hour swim. Visitors learn about dolphin intelligence, habits, and what to expect during the swim. Since swimmers wear masks, fins, and snorkels, they must be good swimmers. Children must be at least 12 years old to participate. There are also half-day, full-day, and scuba diving programs at varying prices.

Leisure

CLOSE ENCOUNTERS OF THE DOLPHIN KIND

The basic message: We were there so the dolphins could play with us. If they didn't feel like playing, we were out of luck. We were warned that a dolphin might put its mouth around an arm or leg—and not to jerk it away. The best way to play was to dive, swim, and

whizzed by. Eagerly, I dove underwater to try to convince the dolphins I was worthy of attention. No go. Another gray flash, this time closer. I picked up my head to see three of the dolphins clustered around one of the swimmers, fascinated by his wristwatch. I floated face down and Sarah came by, hovering



generally act like dolphins.

On my dolphin swim-with, three of us—programs are limited to four people with four dolphins—gingerly entered the water and tried to "play dolphin." We dove and swam underwater, hearing the clicks and whistles that dolphins use to communicate. At first, there was nothing. Then two gray flashes

for moments that seemed to last forever. She sped off but returned, and this time I gently held out my hand to touch her smooth side. More whistles, clicks, and flashes as we tried a water version of tag—and too soon, the 30 minutes were over.

The other program I tried, at Hawk's Cay Resort & Marina (305 743-7000) on Duck Key, was highly structured. Run by Zoovet, which trains

dolphins for shows, this encounter is available only to guests of the upscale resort. After a brief introduction, guests don life vests and become part of the show. As the guests lie near the water's edge, the dolphins give each a "kiss" and are promptly rewarded. The highlight is the dorsal tow. Guests grasp the fins of two dolphins and "ride" between them to the other end of the pool.

I held a hoop for one of the dolphins to jump through, petted them as they swam by, and went on a second dorsal tow. After each task, the dolphins were rewarded with fish. Following the encounter, guests could ask questions of the trainers.

This encounter was more fun but somehow less personal: It was just the dolphins' job. And at the end of the day, it wasn't the thrill of the dorsal tow or the amazement of the hoop jump I remembered—it was Sarah's smile.

Here's a rundown on other dolphin programs:

Dolphin Research (305 289-1121). Includes an hour walking tour/orientation and a 20-minute structured swim; reserve a month ahead. Also available are five- and seven-day "dolphin labs" that offer more extensive seminars, workshops, and contact.

Theatre of the Sea (305 664-2431). Includes a half-hour orientation and 30-minute swim. Half the swim is structured, with dorsal tows; half is "free" time.

Hyatt Regency Waikoloa (800 228-9000). Hotel guests get preference for these sessions; half-hour orientation and emphasis on natural encounters. *Gail DeGeorge*

Worth Noting

FREE LUNCH. Until April 31, Diners Club and American Express cardholders get \$5 off any restaurant meal they charge, provided they aren't already en-

rolled in the cards' bonus-point programs. Those already enrolled won't get rebates but will earn triple bonus points for every meal purchased with either card.

OLD STUFF. Architectural antiques dealer John Wilson, of Santa Monica, Calif., will

issue his first "order by mail" catalog in April. The \$5 booklet (800 331-6599) displays such things as stained-glass windows, art nouveau statues, carved-oak mantelpieces, and stone gargoyles taken from renovated mansions and demolished hotels.

THREE-IN-ONE. Why not have it all? Panasonic's KX-F120 is a telephone, answering system, and fax machine all in one. It's \$1,395 at most major electronic appliance stores. Brother's similar three-in-one Fax 175 lists for \$1,995.

Index to Companies

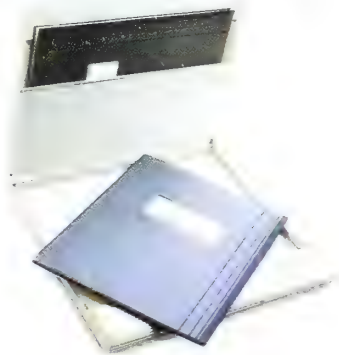
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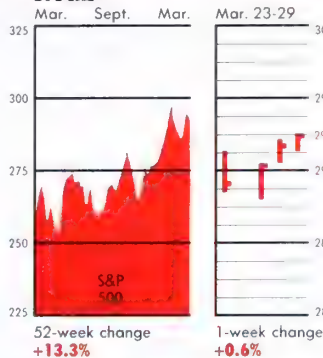
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Investment Figures of the Week

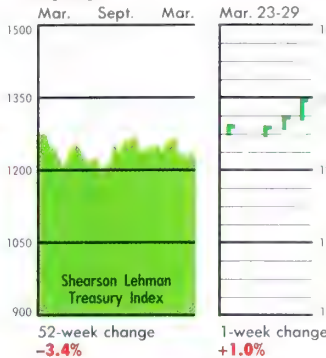
CURRENCY

U.S. dollar bill rates continued to rise and hit a four-year high. Increased demand for dollars, along with a sharp rally for the greenbacks, also gained in price, as long-term interest rates eased in the fixed-income market. The decline in the index of the dollar and the rising indicators. Stocks rose in sympathy, but the big action was in Japan. The Tokyo market racked up over 1,000 points in two days. The Nikkei is now at an all-time high—expected to go higher.

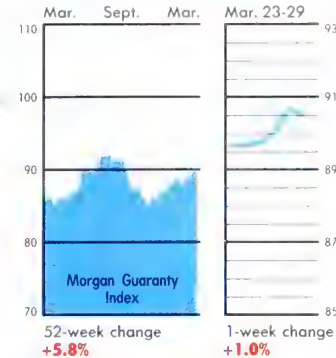
STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS	Latest	% change Week	% change 52-week
ONES INDUSTRIALS	2281.5	0.8	15.3
MPANIES (Russell 1000)	154.6	0.6	12.8
COMPANIES (Russell 2000)	156.8	0.5	12.0
MPANIES (Russell 3000)	166.1	0.6	12.7

IN STOCKS	Latest	% change (local currency) Week	% change 52-week
N (FINANCIAL TIMES 100)	2071.7	1.1	17.9
(NIKKEI INDEX)	32,737.3	4.1	24.4
TO (TSE COMPOSITE)	3560.9	0.1	7.8

FUNDAMENTALS	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	9.3%	9.0%	5.7%
30-YEAR TREASURY BOND YIELD	9.1%	9.2%	8.8%
S&P 500 DIVIDEND YIELD	3.7%	3.6%	3.5%
S&P 500 PRICE/EARNINGS RATIO	11.8	11.7	14.9

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 26-week moving average	282.4	281.6	Positive
Stocks above 26-week moving average	55.5%	56.6%	Neutral
Speculative sentiment: Put/call ratio	0.29	0.30	Neutral
Insider sentiment: Vickers sell/buy ratio	1.31	1.12	Positive

INDUSTRY GROUPS

WEEK LEADERS	% change 4-week	% change 52-week	Strongest stock in group	% change 4-week	% change 52-week	Price
IND GAS DRILLING	12.5	-3.1	HELMERICH & PAYNE	14.8	6.3	25¼
	12.4	40.4	TONKA	30.6	18.1	13⅞
UFACTURED HOUSING	10.4	41.2	SKYLINE	13.3	25.4	19⅞
ITAL MANAGEMENT	8.8	32.5	AMERICAN MEDICAL INTL.	21.8	43.0	21⅞
VELL EQUIPMENT AND SERVICES	8.7	1.3	BAKER HUGHES	14.0	0.7	17¼
WEEK LAGGARDS	% change 4-week	% change 52-week	Weakest stock in group	% change 4-week	% change 52-week	Price
REIGHT	-10.3	0.2	FEDERAL EXPRESS	-11.1	-5.3	45
MINING	-8.8	3.3	NEWMONT MINING	-13.1	11.7	38¼
KING	-6.6	-5.5	YELLOW FREIGHT SYSTEM	-9.9	-10.6	26¼
UMENTATION	-6.3	-11.8	HEWLETT-PACKARD	-6.8	-14.2	51¼
	-6.2	9.9	INLAND STEEL	-10.4	24.7	39¾

MUTUAL FUNDS

RS	%	LAGGARDS	%
4-week total return		Four-week total return	
STRATEGIC INVESTMENTS	14.4	STRATEGIC GOLD/MINERALS	-9.3
ED SERVICES GOLD SHARES	11.3	FIDELITY PACIFIC BASIN	-7.6
TY STRATEGIES	7.2	JAPAN	-7.3
52-week total return		52-week total return	
FMANN	56.8	STRATEGIC INVESTMENTS	-19.4
TY STRATEGIES	36.1	STEADMAN OCEANOGRAPHIC TECHNOLOGY	-17.4
EL CAPITAL APPRECIATION	33.2	STRATEGIC GOLD/MINERALS	-17.3



RELATIVE PORTFOLIOS

Amounts at the present of \$10,000 and one year each portfolio	Foreign stocks	U. S. stocks	Money market fund	Treasury bonds	Gold
ages indicate total returns	\$12,021 +0.25%	\$11,605 +0.58%	\$10,656 +0.16%	\$10,353 +1.26%	\$8,693 +0.21%

on this page are as of market close Wednesday, Mar. 29, 1989, unless otherwise indicated. Groups include S&P 500 companies only; performance and share prices are as of market close.

Mar. 28 Mutual fund returns are as of Mar. 24. Relative portfolios are valued as of Mar. 28. A more detailed explanation of this page is available on request.

PUSH THIRD-WORLD DEBTORS TO CLEAN HOUSE

Now that the U.S. has finally accepted the need for realistic action to reduce Third World debt, it's well to remember that many of the debtors' problems are self-inflicted. In too many countries, production is discouraged and resources squandered by self-defeating and demagogic economic policies. The damage is particularly apparent in the appalling deterioration of basic infrastructure in much of Latin America, where impassable roads, inadequate water supplies, and overloaded communications systems darken the prospect for productive investment.

Debt burdens have exacerbated these problems, but all too often the underlying causes are to be found in patronage-bloated bureaucracies, massive graft, overvalued currencies, and politically motivated government investments in money-losing ventures. In most developing countries, markets are distorted by import protection for inefficient domestic producers and government favors for influential economic groups. Infrastructures decay because politicians frequently keep user charges too low to pay for upkeep and expansion of services.

When they recycled petrodollars to the Third World, the commercial banks turned a blind eye to such practices. In the past, the large international lending agencies tended to make macroeconomic belt-tightening, rather than microeconomic reform, a condition for aid. The affluent nations providing help under the Brady plan should do more. They should insist that the debtor countries tackle the deep-rooted, pernicious, economic and political practices that make their current plight seem so intractable.

DON'T LET DETROIT OFF THE HOOK, MR. BUSH

President Bush is about to face the first major test of his campaign pledge to show more concern for the environment. An array of federal agencies are asking him to reimpose strict fuel-economy standards on U.S. auto makers that would require their fleets to average 27.5 miles per gallon in the next model year. The antiregulation Reagan Administration routinely relaxed such rules on the grounds that consumer preferences rather than government fiat should guide market decisions. But now the Transportation Dept., the Environmental Protection Agency, and the Energy Dept. all agree that this laissez-faire approach is contrary to the national interest.

Their concerns are obvious. Fuel efficiency is declining again, and the price of petroleum is soaring at the same time that the U.S. is becoming dangerously reliant on imported oil—trends that are aggravating the trade deficit. Meanwhile, the damage to the environment from burning fossil fuels is becoming more and more apparent, and many observers believe that over the long run the days of

the gasoline-fueled combustion engine may be numbered.

The Big Three auto makers, who have been pulled mightily from the trend back toward big cars, are understandably reluctant to shift their course again. But the handwriting is on the wall, and they would do well to recognize it before they are confronted with even more stringent fuel efficiency and emission standards. President Bush should lead the way by refusing to relax the rules again.

THE FED CAN'T LICK INFLATION SINGLE-HANDEDLY

Unwelcome as it is, the latest quickening of inflation has one saving grace: It exposes the irresponsibility of the Administration and Congress. By avoiding hard economic decisions, they are increasing the risks of a catastrophic recession. The Administration has been projecting a wildly optimistic economic scenario in which continuing strong growth (aided by creative bookkeeping) provides the revenues to painlessly reduce the budget deficit while inflation cools, interest rates decline, and the deficit narrows. Meanwhile, political expediency has kept the Democratic Congress from pushing its own policy initiatives.

That leaves the Federal Reserve, which has been steady and rightly pushing up interest rates over the past year in an effort to forestall the kind of price surge now under way. But uncertainties and conflicting concerns limit the Fed's powers and policy options. Too much monetary restraint, and who knows what is too much?—could tip the economy into recession and resurrect the specter of \$200 billion deficits. It could also retard progress in narrowing the budget gap by putting undue upward pressure on the dollar. To exercise little restraint risks a disastrous inflationary blowoff exacerbated by a free-falling dollar. And if a recession results in huge debt loads of business and consumers and the inability of the deficit-laden federal government to resort to countercyclical fiscal stimulus suggest that it could prove far more severe than many observers anticipate.

What's more, relying on monetary policy worsens the budget deficit. Economists calculate that each percentage point rise in interest rates adds some \$10 billion to \$12 billion to both the cost of the savings and loan bailout and the annual interest paid on the federal debt. According to the latest projection, higher interest rates could well boost the 1990 budget deficit by \$20 billion or more.

The challenge facing Washington is to reduce the budget deficit while fostering the shift from an economy supported by consumption to one led by exports and investment. That is the only kind of environment in which the Fed and Greenspan can safely allow interest rates to decline. Spending limits are part of the answer, but so are higher taxes aimed at consumption. At the very least, the excise taxes on tobacco, alcohol, and gasoline should be increased. It is ironic that virtually all of the major industrial nations—including Japan and Germany—have followed America's lead by cutting marginal income tax rates, but the U.S. is the only industrial power that has not acted to raise consumption taxes at the same time.



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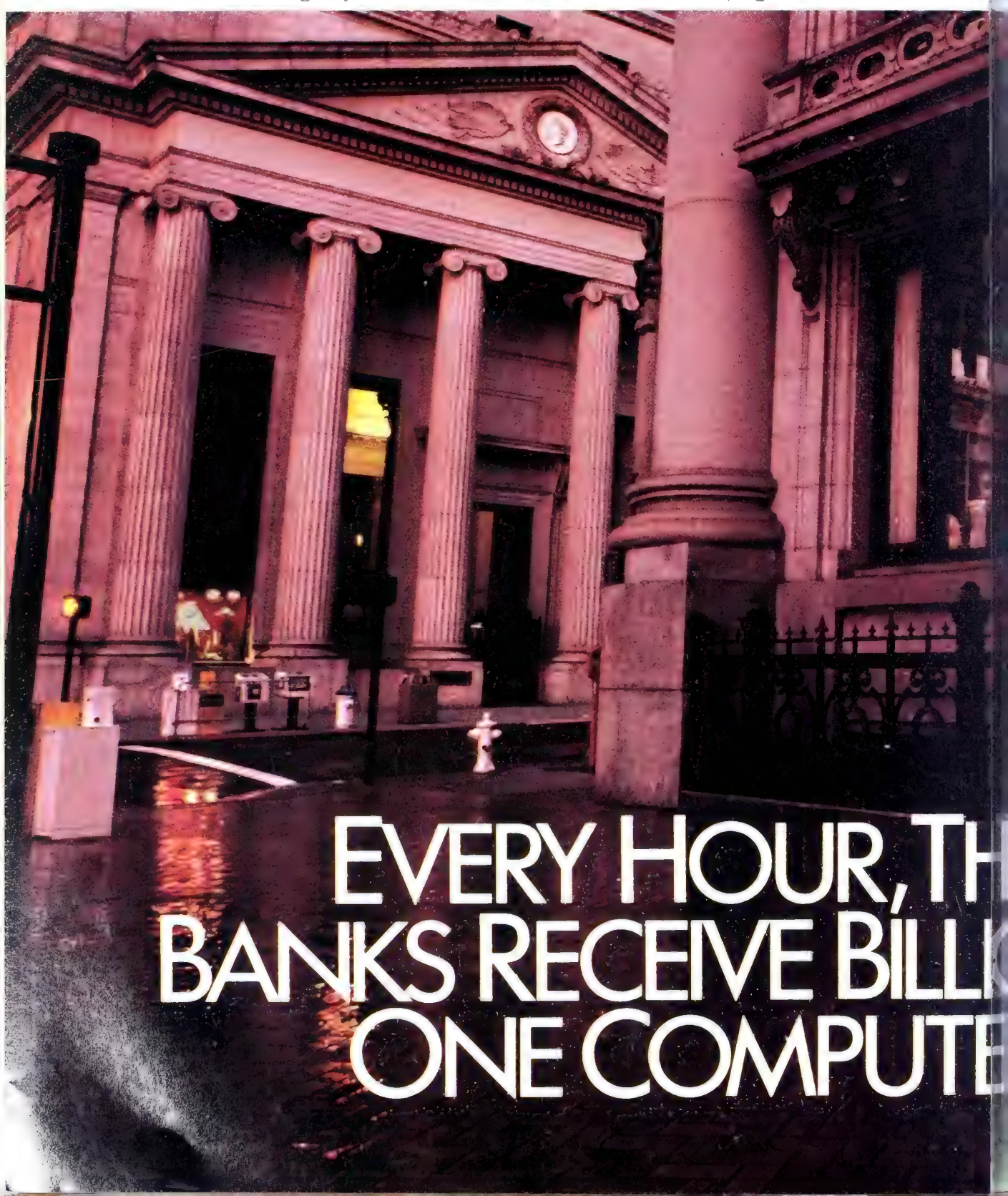
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BEAR TRACKS: UNDISMAYED, FIDELITY IS BUILDING ITS DISCOUNT BROKERAGE IN A BET THAT SMALL INVESTORS WILL RETURN EN MASSE

Cover Story

68 FIDELITY FIGHTS BACK

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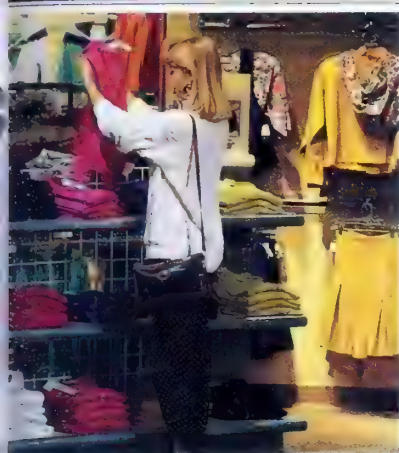
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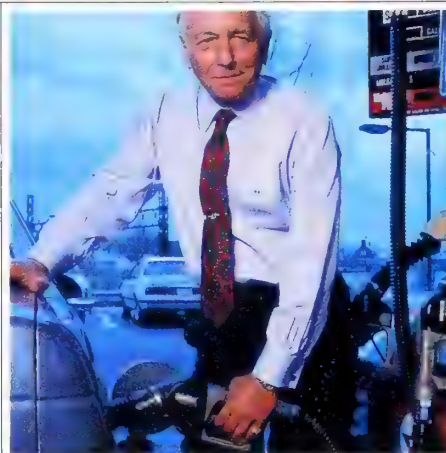
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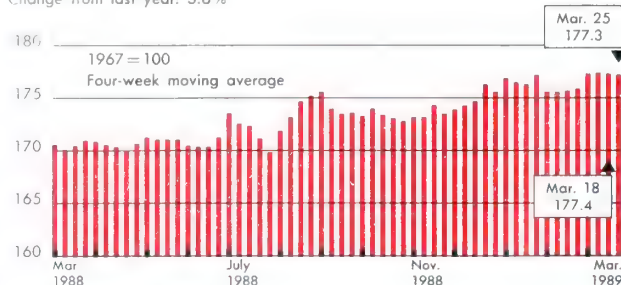
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Keep the Milken case in perspective
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BusinessWeek Index

PRODUCTION

Change from last week: -0.1%
Change from last year: 3.6%

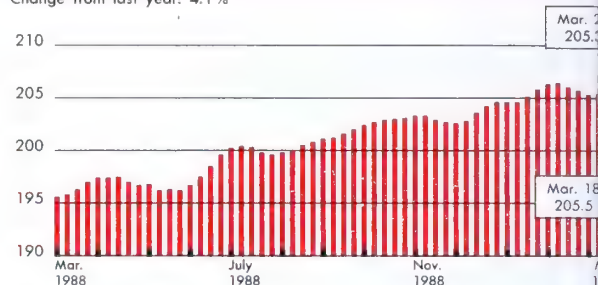


The production index remained virtually unchanged for the week ended Mar. 25. The index has been flat for all of March. On a seasonally adjusted basis, output of coal, autos, paperboard, trucks, electric power, steel, and crude-oil refining increased, while rail-freight traffic, paper, and lumber production posted declines. Before calculation of the four-week moving average, the index rose to 176.7 from 176.5 in the previous week.

BW production index copyright 1989 by McGraw-Hill Inc.

LEADING

Change from last week: -0.1%
Change from last year: 4.1%



The leading index declined slightly for the week ended Mar. 25. On the negative side were lower stock prices, higher bond yields, slower growth in material prices, and a large increase in the number of business failures. These indicators of the positive signs given by faster growth in real estate loans and M2. Prior calculation of the four-week moving average, the index slipped to 205.1 from 205.5 in the week before.

Leading index copyright 1989 by Center for International Business Cycle Research

PRODUCTION INDICATORS

	Latest week	Week ago	% Change year ago
STEEL (4/1) thous. of net tons	2,030	2,097 #	2.8
AUTOS (4/1) units	132,420	127,502r #	10.5
TRUCKS (4/1) units	72,972	71,642r #	10.8
ELECTRIC POWER (4/1) millions of kilowatt-hours	49,132	51,637 #	3.7
CRUDE-OIL REFINING (4/1) thous. of bbl./day	13,463	12,748r #	3.1
COAL (3/25) thous. of net tons	19,896 #	19,934	1.6
PAPERBOARD (3/25) thous. of tons	753.4 #	713.6r	-0.3
PAPER (3/25) thous. of tons	760.0 #	775.0r	1.2
LUMBER (3/25) millions of ft.	483.4 #	481.5	-8.9
RAIL FREIGHT (3/25) billions of ton-miles	19.2 #	20.0	-1.0

Sources: American Iron & Steel Inst., Ward's Automotive Reports, Edison Electric Inst., American Petroleum Inst., Energy Dept., American Paper Inst., WWPAA¹, SFA², Association of American Railroads.

FOREIGN EXCHANGE

	Latest week	Week ago	Year ago
JAPANESE YEN (4/5)	132	133	125
GERMAN MARK (4/5)	1.87	1.89	1.67
BRITISH POUND (4/5)	1.70	1.69	1.88
FRENCH FRANC (4/5)	6.31	6.39	5.67
CANADIAN DOLLAR (4/5)	1.19	1.19	1.25
SWISS FRANC (4/5)	1.64	1.65	1.38
MEXICAN PESO (4/5) ³	2,397	2,392	2,300

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound expressed in dollars.

PRICES

	Latest week	Week ago	% Change year ago
GOLD (4/5) \$/troy oz.	383.000	382.950	-14.9
STEEL SCRAP (4/4) #1 heavy, \$/ton	118.00	118.00	-0.8
FOODSTUFFS (4/3) index, 1967=100	225.5	231.5	3.3
COPPER (4/1) ¢/lb.	143.4	145.1	26.1
ALUMINUM (4/1) ¢/lb.	93.5	90.0	-18.7
WHEAT (4/1) #2 hard, \$/bu.	4.48	4.53	44.5
COTTON (4/1) strict low middling 1-1/16 in., ¢/lb.	58.79	58.57	-2.0

Sources: London Wed. final setting, Chicago mkt., Commodity Research Bureau, Metals Week, Kansas City mkt., Memphis mkt.

LEADING INDICATORS

	Latest week	Week ago	% Change year ago
STOCK PRICES (3/31) S&P 500	292.38	290.18	
CORPORATE BOND YIELD, Aaa (3/31)	9.88%	9.85%	
INDUSTRIAL MATERIALS PRICES (3/31)	104.9	104.3	
BUSINESS FAILURES (3/24)	297	268	
REAL ESTATE LOANS (3/22) billions	\$314.3	\$314.0	
MONEY SUPPLY, M2 (3/20) billions	\$3,089.0	\$3,082.4r	
INITIAL CLAIMS, UNEMPLOYMENT (3/18) thous.	322	336	

Sources: Standard & Poor's, Moody's, Journal of Commerce (index: 1980=100), D. Bradstreet (failures of large companies), Federal Reserve Board, Labor Dept. CIBCIR seasonally adjusts data on business failures and real estate loans.

MONTHLY ECONOMIC INDICATORS

	Latest month	Month ago	% Change year ago
PURCHASING MANAGERS' INDEX (Mar.)	50.4%	53.0%	6.1
AGRICULTURAL PRICES (Mar.) index, 1977=100	149	148	4.1
CONSTR. SPENDING (Feb.) annual rate, billions	\$423.0	\$422.8r	7.1
MANUFACTURERS' INVENTORIES (Feb.) billions	\$359.1	\$357.5r	7.1

Sources: National Association of Purchasing Management, Dept. of Agriculture, Census Bureau, Commerce Dept.

MONETARY INDICATORS

	Latest week	Week ago	% Change year ago
MONEY SUPPLY, M1 (3/20)	\$786.8	\$784.1r	2.1
BANKS' BUSINESS LOANS (3/22)	312.2	311.8	5.1
FREE RESERVES (3/29)	339	410r	-9.1
NONFINANCIAL COMMERCIAL PAPER (3/22)	112.9	113.2r	8.1

Sources: Federal Reserve Board (in billions, except for free reserves, which are expressed in a two-week period in millions).

MONEY MARKET RATES

	Latest week	Week ago	% Change year ago
FEDERAL FUNDS (4/4)	9.52%	9.88%	6.1
PRIME (4/5)	11.50	11.50	8.1
COMMERCIAL PAPER 3-MONTH (4/5)	9.87	10.08	6.1
CERTIFICATES OF DEPOSIT 3-MONTH (4/5)	10.00	10.20	6.1
EURODOLLAR 3-MONTH (3/29)	10.31	10.30	6.1

Sources: Federal Reserve Board, First Boston

Raw data in the production indicators are seasonally adjusted in computing the BW index (chart); other components (estimated and not listed) include machinery and defense equipment. 1 = Western Wood Products Assn. 2 = Southern Forest Products Assn. 3 = Free market value NA = Not available r = revised NM = Not meaningful

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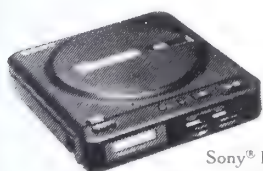
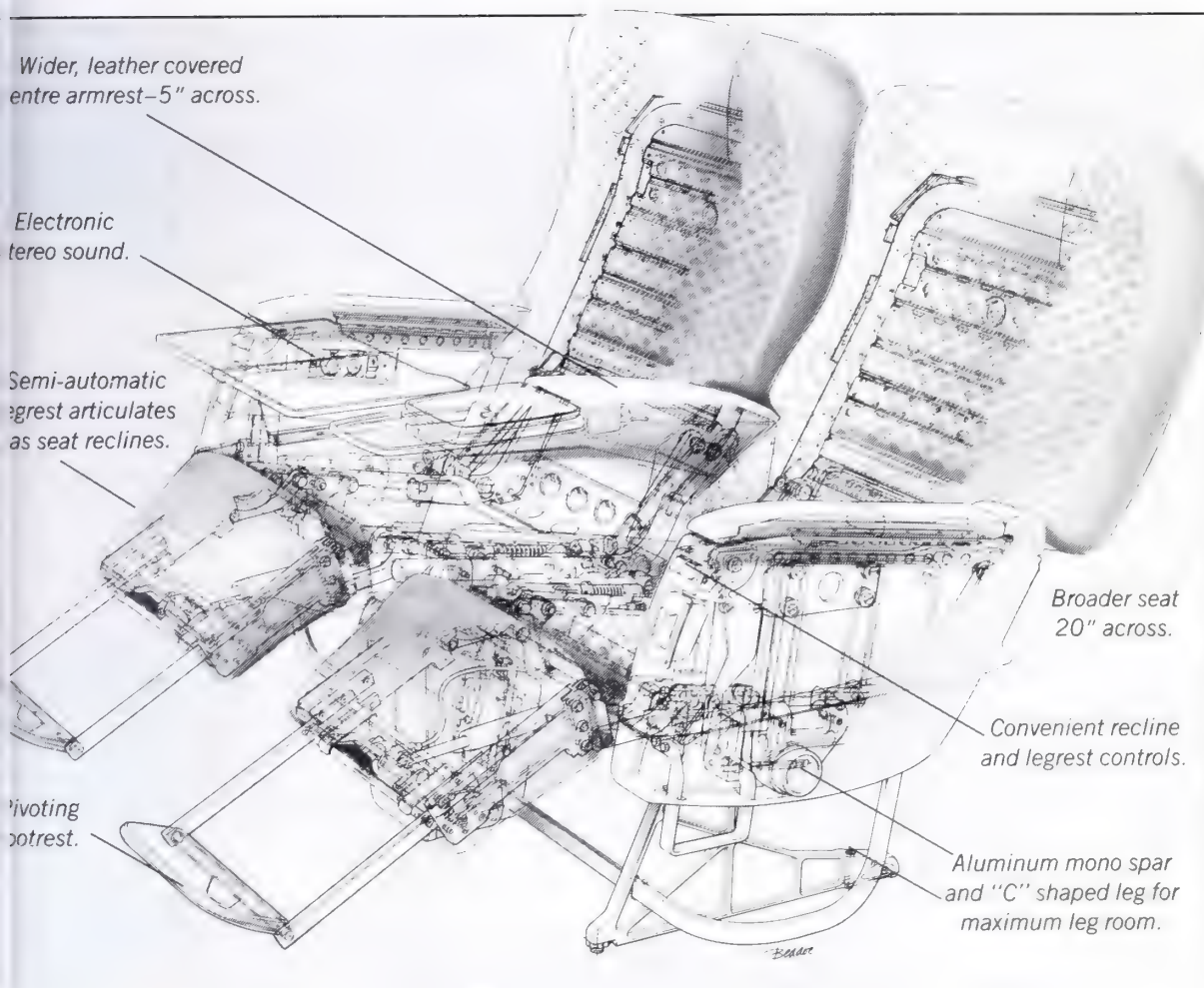
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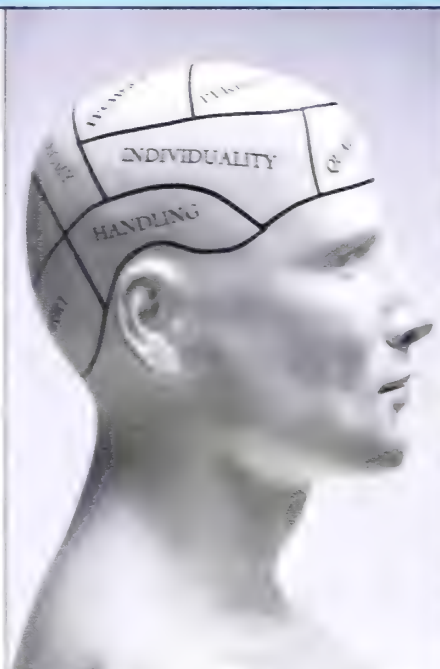
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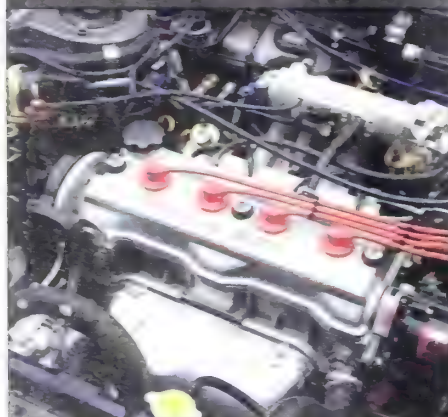
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feet. This extensive area is easily re-
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fold-down rear seat on the hatchback and
split folding rear seat on the sedan.
From front seat headroom, 38.3", 17.2 cubic foot of hatchback cr-
space, Prizm sets new standards of
carrying efficiency.

STRONG POINT



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"tuned" 4-wheel independent suspension,
front disc rear drum brakes, and preci-
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**DID WE SAY 'MOMMY TRACK'?
MAKE THAT 'PARENT TRACK'**

Trying to balance family life and modern corporate life is a problem of increasingly large proportions, whether one is a mommy or a daddy ("The mommy track," Cover Story, Mar. 20). However, the fact that we call it the mommy track says more about how we think about the roles of men and women, in and out of the corporation, than all the laws and policies we have written about gender equality. As long as we label care, consideration, and concern for one's family life "the mommy track," we discourage men from taking an active part in the construction and maintenance of the family.

The primary thrust of all our efforts at obtaining gender equality in the workplace has been toward encouraging women to fill more traditional male roles. Equality, both in and out of the workplace, will not occur until we make an equally concerted effort to encourage men to fill more traditional female roles.

When that happens, we can call it "the parent track." We also may recognize that people who place their priorities on family life aren't being sidetracked, but have only chosen a different career. At that time, maybe parenthood will be recognized as a valued profession, as personally rewarding as any slot in the corporate hierarchy.

John E. Matz Jr.
Holliston, Mass.

Thank you, thank you for the "mommy track" article. Its insight helped clarify my worst fears and my happy choice of being on the mommy track myself.

Driving ambition and a mother's love are a tricky combination. How can we help nurture for the ultimate good of both business and family? You asked women what they thought and got an

earful. Do we dare to ask more men? I hope this isn't a women's issue forever. Congratulations on a must-read piece. I'm sending a copy to my favorite former bosses. Dear CEO...

Joanne Henry
President
Henry Communications
Edina, Minn.

Ipicked up your magazine on the way to work this morning and read your article on the subway. Not long after I got to work, my son's nursery school teacher called to say my son was miserable, in tears, and running a fever.

Could I come fetch him? I had a lot to get done that day, and my panic was drowning out my pity for my son. I tried to reach his nanny, who normally picks him up at noon, but she wasn't home. Nor was a friend and neighbor who has rescued us on similar occasions. Then I called my husband, and they called him out of a meeting across town. "No problem," he said. "Call the school and tell them I'll be there in 20 minutes." In fact, it probably was a problem, inconveniencing people at the meeting and setting the goals of the day back a bit. We take turns at these episodes and sometimes argue about whether his meeting or my deadline is more important. But despite a culture that thinks his job is more important than mine, he tries hard to do his share.

All those women in your article with part-time jobs made me envious. It would be so much easier to work part-time, and I wouldn't miss out on so much or feel so guilty about never volunteering to help the teacher out on field trips to the aquarium. Alas, I have a great job with an employer that has no mommy track. But somehow, all this talk about mommies is missing the point. What about all those daddies?

My husband missed his meeting, but he arrived to the hugs and whimpers of a sick child. Mothers should not have to



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Readers Report

choose between jobs and children, but neither should fathers. Men and the workplaces they still largely rule should

Renee Boicourt
New York

What ever happened to the women's movement, editors? The attitude pervasive in your story indicates that you have forgotten it ever happened. What about a people track? Haven't we made any progress in your eyes? Your treatment of the issue belongs in the '50s.

Even your graphics are sexist and inappropriate. Surely there are at least one or two fathers in America who participate in alternative career paths, extended leave, flexible scheduling, job sharing, and telecommuting.

Sally Giddens
Associate Editor
D. the City Magazine of Dallas
Dallas

I put myself on the daddy track seven years ago, giving up a solid corporate career for a home-based consulting practice. Although my income dropped for a while, my quality of life skyrocketed.

Some of my male peers snickered, but most were, and remain, openly envious.

This solution suited me, but there are many alternatives that let people blend work and family needs. These needs don't have to be mutually exclusive if employers selectively offer job sharing, telecommuting, part-time work, and other proven, manageable options.

Companies fearful of opening Pandora's box by offering these options should realize that fewer and fewer people want to play by the rules of the traditional career game. Some of those who do may be good corporate lieutenants but are hardly the leaders we sorely need in business today.

Gil E. Gordon
Editor

Telecommuting Review
Monmouth Junction, N. J.

I took great offense at the fourth paragraph, beginning: "Reshaping work to help a woman raise a family..." That lead encapsulates the very root of the problem. Until society as a whole can truly embrace the notion that the task of raising a family is a responsibility shared between the parents, no amount of reshaping will have satisfactory ef-

fect. Why must it be only the woman with the dual role? Pregnancy (and aging) is only a few months in the life of a child-rearing process.

Leigh Watson Mendenhall
Boulder, CO

WHY MANY OF THE UNEMPLOYED ARE GOING TO STAY THAT WAY

The economists cited in your article "Plenty of workers are waiting for the wings" (*Economics*, Mar. 13) are leading American companies.

Yes, there may be many able-bodied people who are not currently working, but many are not available for jobs, especially for jobs that need to be filled.

Labor, unlike potatoes or any other commodity, is not an undifferentiated source. If there are 30 million Americans out there, many are too advanced in their careers to find attractive the entry-level jobs that are so abundant. A 40-year-old mechanical engineer who is laid off by his Rust Belt employer will not move gladly into an entry-level, technical-services job on the West Coast.

Moreover, our studies show that many of the retired or elderly who want to work are time jobs are working. The same is true

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mothers and homemakers. The hard-unemployed need significantly more before they can be integrated into economy.

The story also incorrectly leads readers to believe that wages haven't increased. Wages in tight segments, particularly at the entry level, have soared. These include career-starting jobs, just "hamburger-flipping kids." The wages show little increase because sizable increases at the entry level have been offset by compression occurring with midlevel salaries.

Martin M. Greller, President
Personnel Strategies Inc.
Warren, N. J.

'S NOT FORGET IT BOYD BUILT JEFFERIES

How sad I was to read "Life after Boyd? And how" (Finance, Mar. Success didn't come overnight to Jefferies & Co. My husband spent 25 years building sound relationships with 400 or so employees and their families and his many clients worldwide. Fortunately, this sound base has been able to survive and grow. His total dedication to his clients' demands, and the petition, made him make an error in judgment that he deeply regrets. Boyd

CORRECTIONS

In BUSINESS WEEK's Apr. 3 Bank Scoreboard, data supplied by Keefe, Bruyette & Woods Inc. incorrectly included Sunwest Financial Services Inc. among banks showing large declines in adjusted earnings per share during 1988. Sunwest's 1988 earnings were \$2.50, not \$0.25 as Keefe Bruyette reported.

In "Japan's telephone colossus takes its first baby steps overseas" (Special Report, Mar. 13), comments regarding the plans and prospects of NTT International Corp. should have been attributed to Ichiro Yamanouchi, the company's president. Because of an editing error, they were attributed instead to Haruo Yamaguchi, the president of Nippon Telephone & Telegraph, NTT International's parent company. Also, the \$1.8 billion in earnings NTT expects for fiscal 1989, ended Mar. 31, is after taxes, not before.

Jefferies has had a very positive influence on the marketplace and will continue to be respected by those who know him well.

Sharon K. Jefferies
Aspen, Colo.

O.K., LOGIC BUFFS, TRY THIS ONE

Regarding your review of John Allen Paulos' book *Innumeracy: Mathematical Illiteracy and its Consequences* ("America + math phobia = big trouble," Books, Feb. 20): Question 2 is fine, and Answer A is correct, but the explanation is wrong. It is true that "a single statement is always more probable than both of two statements" only when one of the two statements is the same as the single statement. For example, the single statement "Judy works as a bank teller" may be less likely than the two statements "Judy is employed and a registered voter."

I believe the correct explanation would be "it is always more likely that a single statement is true than that the same statement and a second statement are both true."

Michael J. Cullender
AT&T Information Systems
San Antonio

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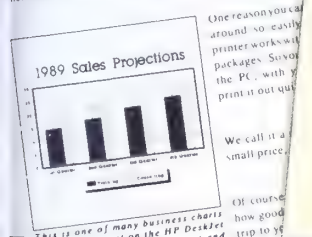
But they keep looking at the evidence.

HEWLETT
PACKARD

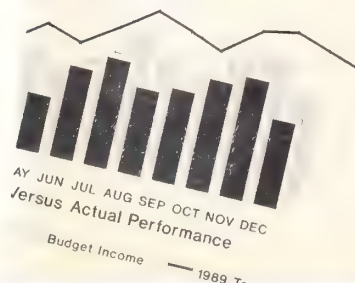
Arnold R. Jones
Bush Street, Suite 845
San Francisco, CA 94104

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WHEN THE MACHINE STOPPED: A CAUTIONARY TALE FROM INDUSTRIAL AMERICA

By Max Holland

Harvard Business School Press • 335pp • \$22.95

AN AMERICAN TRAGEDY: HOW A GOOD COMPANY DIED

The Rust Belt is back. So say bullish observers as U.S. exports surge, long-moribund industries glow with newfound profits, and unemployment dips to lows not seen in a decade. But in the smokestack citadels, there's disquiet. Too many machine-tool and auto-parts factories are silent; too many U.S. industries still can't hold their own.

What went wrong since the heyday of the 1960s? That's the issue Max Holland, a contributing editor of *The Nation*, takes up in his nutsy-boltsy but fascinating study *When the Machine Stopped*.

The focus of the story is Burgmaster Corp., a Los Angeles-area machine-tool maker founded in 1944 by Czechoslovakian immigrant Fred Burg. Holland's father worked there for 29 years, and the author interviewed 22 former employees. His shop-floor view of this small compa-

ny is a refreshing change from academic treatises on why America can't compete.

The discussions of spindles and numerical control can be tough going. But Holland compensates by conveying the excitement and innovation of the company's early days and the disgust and cynicism accompanying its decline. Moreover, the fate of Burgmaster and its brethren is crucial to the U.S. industrial economy: Any manufactured item is either made by a machine tool or by a machine made by a machine tool.

Producing innovative turret drills used in a wide variety of metalworking tasks, Burgmaster was a thriving enterprise by 1965, when annual sales amounted to about \$8 million. The company needed backing to expand, however, so it sold out to Buffalo-based conglomerate Houdaille Industries Inc. Houdaille was in

turn purchased in a 1979 leveraged buyout led by Kohlberg Kravis Roberts & Co. By 1982, when debt, competition and a sickly machine-tool market battered Burgmaster badly, Houdaille went to Washington with a petition to withhold the investment tax credit on certain Japanese-made machine tools.

Thanks to deft lobbying, the Senate passed a resolution supporting Houdaille's position, but President Reagan refused to go along. Houdaille's subsequent attempt to link Burgmaster with a Japanese rival also failed, and Burgmaster was closed.

Holland uses Burgmaster's demise to explore some key issues of economic and trade policy. Houdaille's charge that a cartel led by the Japanese government had injured U.S. toolmakers, for example, became a rallying point for those who would blame a fearsome Japan for the problems of U.S. industry.

Holland describes the Washington wrangling over Houdaille in painful detail. But he does show that such government decisions are often made without much knowledge of what's going on in the industry. He shows, too, that Japanese producers succeeded less because of government help than because of

NORTHWEST

THERE'S NOTHING SIMPLE ABOUT A BUSINESS TRIP TO OSAKA

The complexities of doing business in Osaka can be overwhelming. Not only is the language foreign, but the rituals and business practices are quite different from our own. For this reason, the power of having just a little knowledge beforehand should never be underestimated.

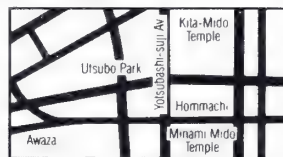
WORD POWER. Try to type up all your ideas and the points you want to make at your meetings, so you can hand it out before you start. The Japanese understand written English much better than they do the spoken word.



DINING FOR DOLLARS.

Kicho is one of the most well-known restaurants in all of Japan. It's also the absolute best, so it's always booked. If you are invited to dine there, cancel all plans and go. 3-23 Korai-bashi, Higashi-ku, Osaka. Tel: 231-1937.

THE PERFECT GIFT. If you need a special gift, try a string of pearls from Mikimoto, 1F Shin-Hankyu Bldg. 1-12-39 Umeda, Kitaku.



OSAKA CENTRAL.

Although friendly, Osaka's taxi drivers speak almost no English, so get all your directions written in Japanese before you leave the hotel. It's an enormous, congested city, so make sure to allow time for traffic delay.

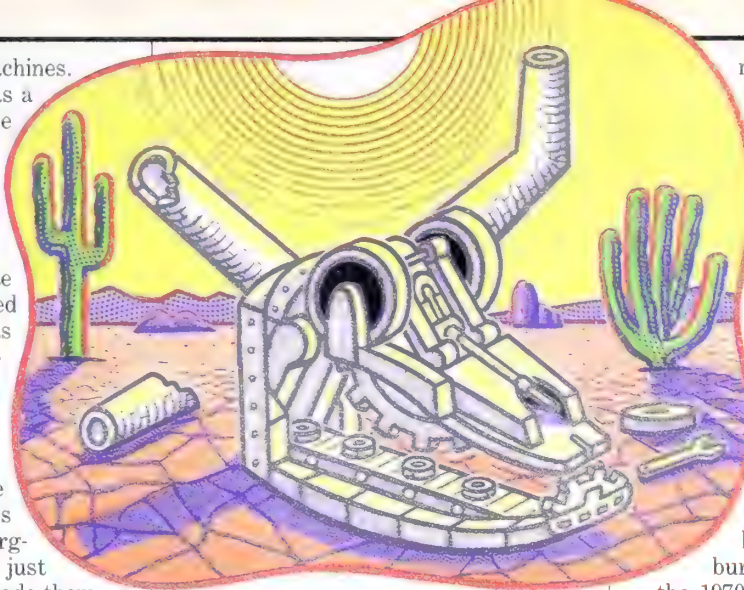
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le better, cheaper machines. or those who see LBOs as a symptom of what ails the economy, Holland offers plenty of ammunition. He argues persuasively that the LBO crippled Burgmaster by creating enormous pressure to generate profits. As Burgmaster pushed products out as fast as possible, he writes, it routinely shipped defective machines. It promised custom features that engineers hadn't yet designed. And though KKR disputes the claim, Holland concludes that the LBO choked off Burgmaster's investment funds just when foreign competition made them necessary. As for Houdaille, it was capitalized and sold to Britain's Tube Investments Group.

But Burgmaster's problems had started even before the LBO. Holland's history of the company under Houdaille is a table catalog of modern management techniques that flopped. One of the most disastrous was a system for commercializing production scheduling that was too crude for complex machine-tool manufacturing. Holland gives a dramat-



ic depiction of supply snafus that resulted in delays and cost increases.

As an independent company, "Burgmaster thrived because the Burgs knew their business," Holland writes. Their departure under Houdaille was followed by an "endless and ultimately futile search for a better formula." But, he concludes: "No formula was a substitute for management involvement on the shop floor."

In the end, however, Holland puts

most of the blame for the industry's decline on government policy. He targets tax laws and macroeconomic policies that encourage LBOs and speculation instead of productive investment. He also criticizes Pentagon procurement policies for favoring exotic, custom machines over standard, low-cost models. This adds up to an industrial policy, Holland writes—a bad one.

The point is well taken, but Holland gives it excessive weight. Like their brethren in Detroit and Pittsburgh, domestic toolmakers in the 1970s were too complacent when imports seized the lower end of the product line. The conservatism that had for years served them in their cyclical industry left them ill-prepared for change. Even now some of the largest U.S. toolmakers are struggling to restructure. Blame the government, yes. But blame the industry, too.

BY ZACHARY SCHILLER
Cleveland Bureau Manager Schiller began writing about machine tools in 1979 by reporting the industry's first trade deficit.

ILLUSTRATION BY PAUL L.



NORTHWEST ASIA SERIES

WANT TO BOOST PRODUCTIVITY? TRY GIVING WORKERS A SAY

BY ALAN S. BLINDER



The solution to America's pathetic productivity growth isn't necessarily more capital spending. Several studies show that giving workers more responsibility can have a marked effect

The nation's chief economic malady today is not the budget deficit, the trade deficit, inflation, or poverty. It is our miserably slow pace of productivity improvement. Since 1973 the volume of output that American businesses get from a typical hour of labor has increased just 1% per year on average. That compares poorly with both the 2.7% annual productivity increments that we enjoyed over the previous 15 years and the roughly 2% growth rate we experienced over the preceding century.

The difference between 1% and 2% productivity growth may not sound like much. But when compounded over a long period of time, it is. At 2% annual growth, real wages double every 35 years; in a century, the standard of living increases more than sevenfold. But at 1% productivity growth, it takes 70 years for real wages to double, and the standard of living less than triples in a century. Clearly, restoring U.S. productivity growth to its historic 2% norm would be a monumental achievement. The question is, can we do it?

Most of the productivity-enhancing policies advocated by politicians, economists, and executives are aimed at quickening the pace of capital formation. The logic is impeccable: With more and better capital to work with, each hour of labor should produce more output. The problem comes with magnitudes. Since capital constitutes only 25% to 30% of the economy's total inputs, even a large increase in investment will yield only small productivity gains.

TEMPTING TARGET. Since it is a much bigger input, labor makes a more tempting target. What can we do to make American labor work harder and better? One simple and inexpensive approach may be to change the way businesses pay their employees. It is not written in stone that workers must be paid straight hourly wages. In fact, scattered pieces of evidence from this and other countries suggest that alternative forms of compensation such as profit-sharing may foster higher productivity.

To investigate this idea more thoroughly, the Brookings Institution asked me to organize a conference, which met last month in Washington. Five papers were presented by experts on their respective subjects. It turned out that the evidence that alternative pay systems raise productivity is stronger than I had imagined. Not only that, but an interesting theme emerged at the conference: Employee participation may be one of the keys to higher productivity.

A new study by Daniel Mitchell, David Lewin, and Edward Lawler not only estimated that productivity is about 5% to 10% higher in companies with profit-

sharing but also found that productivity is higher in enterprises with an organized program of worker participation. Both findings, they noted, accord with earlier evidence.

Martin Weitzman and Douglas Kruse reviewed every statistical study they could find of the effect of profit-sharing on productivity. There were 15 studies in all, and every one suggested a positive effect. Can economic theory explain the phenomenon? Weitzman and Kruse concluded that theory leaves open too many possibilities: Profit-sharing might or might not work depending on accident of history such as the presence or absence of cooperative attitudes and "team spirit." If you listened closely, you could hear the participation theme again.

A paper by Michael Conte and Svejnar concluded that there was no weaker evidence to support the proposition that Employee Stock Ownership Plans raise productivity. Interesting, however, it appears that ESOPs do no good for productivity in companies that have participatory institutions.

CAUSE AND EFFECT. Masanori Hashino analyzed the Japanese system of industrial relations. While he did not claim to have unlocked the secret of Japan's industry's high productivity growth, he emphasized the roles of extensive consultation between labor and management and consensus-based decision-making. Although these cumbersome procedures absorb much time and effort, they seem to bear fruit.

Finally, a paper by David Levine and Laura Tyson examined directly the evidence on participation. They argued that a great deal of admittedly weak evidence from a variety of countries carries a consistent message: Employee participation, if done right, can and does raise productivity.

To me, all this adds up to a strong and rather different message than I expected. While the research is hardly definitive, it now seems a good bet that some form of institutionalized participation by workers can raise productivity as well as increase the effectiveness of other productivity-enhancing measures such as profit-sharing. And it costs little.

Which participatory programs are best? The sketchy evidence points away from giving labor a seat on the board of directors and toward substantive shop floor consultation—something that goes beyond the suggestion box and engages workers in a meaningful way. The appropriate form will no doubt vary from company to company. As several industry and labor representatives pointed out at the Brookings conference, participation, like marriage, works best when both parties want it to work.

ALAN S. BLINDER IS THE GORDON S. REINER CHAIRMAN AND MEMORIAL PROFESSOR OF ECONOMICS AT PRINCETON AND AUTHOR OF *HARD HEADS, SOFT HEARTS*.

A wide-angle photograph of a baseball stadium at night. The stands are filled with a large crowd of spectators. The field is brightly lit, and a large, three-dimensional red "J&B" logo is positioned on the grass near the pitcher's mound. The sky above the stadium is dark with some clouds.

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BY GENE KORETZ

THE TRUE COST OF BORROWING IS HIGHER THAN IT SEEMS

The jury is still out on whether the sharp rise in interest rates over the past year has been enough to restrain inflation and dampen consumer spending. One common theory is that financial deregulation has so blunted the impact of monetary tightening that interest rates must be pushed to Draconian heights before they really bite. Indeed, both short- and long-term rates are still far below the levels that finally quenched inflation in the early 1980s.

Economist Martin H. Barnes of *The Bank Credit Analyst*, a Montreal-based monthly publication that monitors U.S. economic trends, disagrees. "What ultimately affects the economy," he says, "is not the level of nominal interest rates but the cost of credit after inflation and taxes have been taken into consideration." When short-term rates start-

To be sure, whereas Barnes uses the prime rate plus 4% as a proxy for consumer-lending rates, many actual consumer rates have climbed less rapidly than the prime has over the past year. But he points out that they are still up sharply when inflation, lower tax rates, and the loss of tax deductibility are factored into the equation.

"Although most consumers don't calculate the real aftertax cost of borrowing," he says, "it still represents the true burden of debt servicing and thus eventually affects their behavior." And with rates headed higher, Barnes says, "economic growth should slow to a crawl in the second half."

WHY THIS QUARTET IS SINGING THE RECESSION BLUES

The consensus forecast is that the economy this year is headed for a soft landing—that is, a slowdown rather than a recession. But a small group of Wall Street economists think the latest tightening of the monetary screws—combined with evidence of emerging economic weakness—implies that a downturn will start before yearend.

■ Gert von der Linde of Donaldson, Lufkin & Jenrette Securities Corp. thinks we may already be in a recession. He notes that "the major sources of strength in recent years have been the merchandise export boom and the related surge in capital spending, both of which seem to have run out of steam." With inflation-wary nations tightening credit overseas and no growth likely in housing and defense spending, "the U.S. economy can only move in a downward direction," he says.

■ Bruce Steinberg of Merrill Lynch, Pierce, Fenner & Smith Inc. notes that short-term interest rates are up some 330 basis points over the past year—"a larger increase than the rises preceding six out of the last seven recessions." Similarly, cash-flow margins (the ratio of cash flow to corporate output) fell last quarter to levels that have typically preceded past downturns by six to nine months. Meanwhile, "disappointing car sales, the recent sharp drop in computer orders, and sluggish export demand all suggest that we will slip into recession before the end of the year."

■ Burton Zwick of Kidder, Peabody & Co. believes that the pickup in core inflation to about 5% necessitates further Fed tightening that will "reinforce an economic slowdown already under way." Inflation is unlikely to fall to a more acceptable level, he says, unless the Fed

induces a mild recession. And the Fed Administration may tolerate monetary restraint now in the belief that it will allow stronger growth later on.

■ James R. Solloway of Argus Research Corp. thinks growth will turn negative in the second half—and perhaps sooner. High interest rates are affecting housing building and sales of big-ticket durables, he says, while capital spending is slowing, and the strong dollar and credit stringency overseas are stalling foreign trade progress. "The kicker," he says, "is the level of nonfarm inventory accumulation, which is very high in current terms and will quickly become burdensome if demand continues to weaken."

Most economists who expect a downturn think it will be mild. "Inflation is as entrenched as it was in past expansions," explains Solloway, "so the Fed will be able to ease more quickly." Gerd Linde of Donaldson Lufkin is sanguine, however. "The large trade imbalances afflicting the world economy suggest that we may be facing a semi-synchronous contraction," he warns.

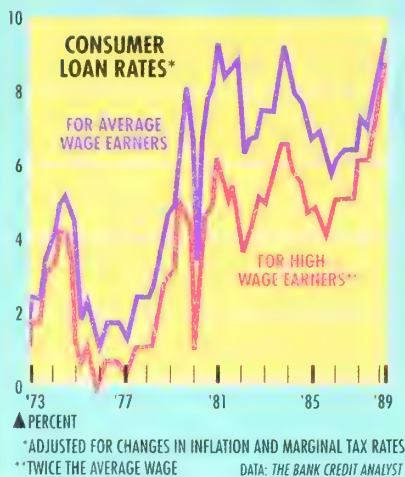
JOE HILL GOES FURTHER OVER THE HILL

The waning power of unions—or the factors limiting U.S. wages—is still apparent in labor statistics. The Labor Dept. reports that this year the unionized share of the nonfarm work force fell to just 16.8%—the lowest reading in more than 50 years. While 37 percent of government employees are union members has stayed around 37% in recent years, the share of private sector workers in unions dropped to 12.9% from 16.8% in 1983. All of which helps explain why there were only two major strikes in 1988, the lowest since record-keeping began in 1947.

WITH TWO GOOD CARS IN MOST GARAGES, WHAT'S DETROIT TO DO?

Will Detroit's latest batch of new cars rev up car sales? Economist Edward E. Yardeni of Prudential-Bache Securities Inc. is skeptical. He notes that 63 million cars were sold from 1980 through 1988 (compared with an 8 million rise in payroll employment). "It may just be that all of America's two-car garages are full of two fairly new cars," he says. "After six years of expansion, the odds are that most of the pent-up demand for autos has been satisfied."

REAL AFTERTAX INTEREST RATES ARE AT A NEW PEAK



ed moving up sharply in the late 1970s, for example, inflation-fueled income gains helped ease the pain for consumers. And because interest payments were deductible, and tax rates were higher than today, aftertax interest costs stayed relatively low.

This time around, however, inflation still hasn't affected wages much, marginal tax rates are down significantly, and the deductibility of nonmortgage interest has been largely phased out. The upshot, says Barnes, is that real aftertax interest rates on conventional consumer loans have now risen to "the most punitive levels of the postwar period."

CATTERED ECONOMIC SHOWERS. ARE THUNDERCLOUDS ON THE WAY?

Dcattered signs of cooler economic growth are starting to appear. That's to be expected as expansions wear on. But in this expansion, the best hint a coming economic slowdown will be a slackening in both domestic and foreign demand. That combination has been the economy's driving force for the past two years.

The fate of domestic demand rests largely with the Federal Reserve Board and its year-long mission to dampen spending with higher interest rates. The jury is still out on that. Most economic data for February looked weak. But that stemmed largely from January's unusually mild weather, which inflated many of the month's numbers and caused many February indicators to pale in comparison. Data for March, now trickling in, and April will give better clues.

For now, construction seems to be the only domestic sector to be hit by higher interest rates. That's especially true for housing. But consumer spending is the best measure of domestic demand. And here, strong growth in jobs and incomes continues to buoy the outlook. What weakness there is in consumer spending is centered in car sales, but higher rates don't seem to be the problem. Car buying has been lackluster despite Detroit's low-interest loans. Aside from cars, spending was healthy last quarter and should remain so this quarter.

INDUSTRY SHOWS SIGNS OF STRAIN

Still, Fed tightening may have had an unintended side effect on foreign demand. Higher U.S. interest rates have strengthened the dollar over the past year, putting a chill on export growth. Manufacturing is feeling some strain: Gains in factory output have slowed, and new orders in both durable and nondurable manufacturing fell in January and February. The National Association of Purchasing Management's index of business activity, heavily slanted toward the industrial economy, reflects the cooler pace in manufacturing. The index, a composite reading of orders, production, employment, inventories, delivery times, and sales, dropped to 50.4% in March (chart). A reading above 50% indicates growth, but this was the lowest since July, 1986—back before the export boom, when factories were languishing as imports flooded in. The slowdown in exports is partly responsible for this quarter's look. After a three-year drop, the dollar has now

risen 8% above its year-ago level. And the NAPM reports that fewer exporting companies are seeing increases in ordering from abroad. In the first quarter, 24% reported gains in foreign orders, down sharply from 37% in the first quarter of last year (chart).

It's difficult to conclude, however, that the industrial sector is in as sad a state as the purchasing managers' index would imply. New orders in January and February are running ahead of the fourth-quarter average, and so is industrial output. Factory work hours have been at a high level. So the NAPM index is likely to rebound.

Part of the industrial slowdown may result from the latest round of weak car sales and the impact this has had on auto production. Car sales in late March were 6.8 million at an annual rate, about the same as in the middle of the month. That was a bit higher than the 6.2 million pace in early March, before Detroit's sales incentives began.

Car buying is settling into a slower growth track after six years of expansion, now that pent-up demand following the 1981-82 recession has been largely filled. Also, car buyers have come to expect ever-bigger discounts on prices and financing.

Since December, car sales have run well below output, making inventories bulge. In an effort to trim stocks, Detroit has cut output sharply, from a 7.9 million annual rate in December to well below 7 million in March.

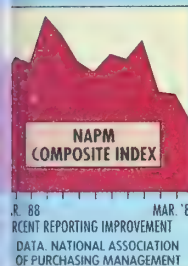
Output cuts of that size also can have temporary impacts on other industries such as steel, rubber, and plastics. In February, for example, manufacturing shipments dropped a steep 1.7%, to \$227.6 billion. And since December, fewer deliveries of automotive equipment have accounted directly for one-third of the loss in shipments. A similar pattern developed in early 1988.

Detroit has further liberalized its deals to include more models with low-rate—and even no-rate—financing, which should help April sales. If so, lower inventories will clear the way for higher output this spring.

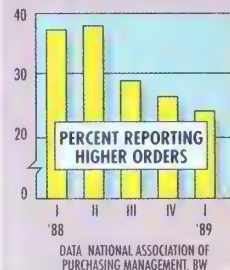
RATES ARE RISING; BUILDINGS AREN'T

If it's hard to pin sick car sales on the Fed's tightening, the effect of higher interest rates on construction is crystal clear. Building has already passed its peak for this business cycle, and contracts for new projects have nose-dived. Construction spending in February stood at an annual rate of \$423 billion, unchanged from

PURCHASERS SEE A SLOWDOWN



EXPORT ORDERS LOSE SOME PUNCH



Business Outlook

January. Outlays in the private sector dipped 0.1%, following a big 1.7% jump in January, but that gain was influenced by the month's mild weather.

Building in February was weakest where rising interest rates were most burdensome. Spending on housing fell 0.2%, and nonresidential construction was 0.3% below January's level, with a 1.9% drop in industrial construction. Public works—which are more dependent on budget appropriations than interest rates—rose 0.7%, with big increases in educational and conservation facilities.

Construction held up surprisingly well last year, despite the increase in interest rates. Spending has risen by 7.8% since February, 1988, and is up 6.9% after changes in prices. In particular, the strong upward trend in real spending on nonresidential buildings means that this part of business investment, which fell 1.1% at an annual rate in the fourth quarter, will add positively to last quarter's gross national product growth.

DEMAND FOR NEW HOMES WEAKENS

For the rest of the year, however, rising rates will take their toll, particularly in housing. Sales of new single-family houses in February were already 4.6% below their year-ago levels, and demand for both new and existing homes in early 1989 has been weak.

In addition, the export-led slowdown in factory output will lessen the need to build new plants. Indeed, even with the increase in industrial operating rates, companies have been reluctant to expand their facilities.

Spending on industrial buildings, after adjusting for inflation, has been flat since mid-1986. During the same time, capacity utilization in manufacturing has risen from 79.7% in 1986 to 84.6% in February, 1989—almost five percentage points. Companies seem to be buying equipment to increase capacity and to improve productivity, but they're not breaking ground for new factories.

Another sign of a coming construction slowdown is the fall in new building contracts. The F. W. Dodge Div.

of McGraw-Hill Information Services Co. reports that new contracts in February declined 7%, to an annual rate of \$233.1 billion. That followed a 5% drop in January placed the value of contracts at its lowest in two years. The big losers were plans for office and industrial projects; each fell 20% in February.

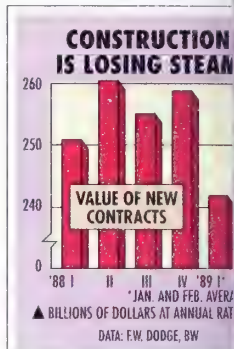
For January and February, new contracts ran at an annual rate 23.7% below their fourth-quarter peak (chart). So, as older projects are completed, there are fewer new ones to pick up the slack. That means construction will drift lower in the second half of the year.

Commercial building is one sector that is sure to suffer. True, construction of offices, stores, and warehouses has been healthy in recent months. Spending for such buildings increased 0.3% in February, following a 3.2% surge in January. But that strength is unlikely to last because of high vacancy rates in office buildings—one-half of all commercial building.

Coldwell Banker Commercial Real Estate Service says that about 16.1% of downtown office space and 21.4% in the suburbs was unoccupied in the first quarter. In Southwestern cities such as Houston, Oklahoma City, and Austin, about a third of all office space is vacant.

Other commercial projects are unlikely to fill the gap. Slower factory growth means fewer warehouses will be needed to distribute goods. And retailers are facing a profit squeeze, partly because of rising costs, which could force them to rethink plans to expand stores.

With construction headed downhill, and with the slowdown in exports starting to cool off the manufacturing sector, consumers are again becoming the expansion lifeline. How hard Fed tightening hits there may well mean the difference between slowdown and recession.



THE WEEK AHEAD

RETAIL SALES

Thursday, Apr. 13, 8:30 a.m.

Retail sales were probably unchanged in March, following a 0.4% drop in February. Sluggish car sales offset gains elsewhere, boosted by an early Easter holiday. For the first quarter, inflation-adjusted retail sales probably fell about 1% at an annual rate.

PRODUCER PRICE INDEX

Friday, Apr. 14, 8:30 a.m.

The consensus is that producer prices of finished goods rose by 0.6% in March. Higher energy prices probably offset a drop in food costs. With the expected rise in March, producer prices likely grew at an annual rate of 9.3% in the

first quarter—the fastest pace in almost eight years. Prices surged 1% in both January and February.

MERCHANDISE TRADE DEFICIT

Friday, Apr. 14, 8:30 a.m.

Most economists project a February trade deficit of about \$10.5 billion. A rise in customs-duty payments suggests that imports increased, probably at a faster rate than exports did. In January the deficit narrowed to \$9.5 billion.

INDUSTRIAL PRODUCTION

Friday, Apr. 14, 9:15 a.m.

Industrial output probably rose by 0.2% in March after posting no change in February. The small gain is suggested by the low 50.4% reading of the business

activity index compiled by the National Association of Purchasing Management.

CAPACITY UTILIZATION

Friday, Apr. 14, 9:15 a.m.

Industrial output's small gain suggests that the capacity-utilization rate ticked up to 84.4% in March. The February industrial operating rate was 84.3%.

BUSINESS INVENTORIES

Friday, Apr. 14, 10 a.m.

Inventories at manufacturers, wholesalers, and retailers most likely grew 0.6% in February, following a 0.7% increase in January. That's indicated by the already reported 0.5% gain in factory stocks and the 0.4% drop in retail sales, which boosted retailers' inventories.

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GETTING BANKS TO JUST SAY 'NO'

THE FEDS STEP UP THEIR CAMPAIGN AGAINST LAUNDERING DRUG MONEY

The numbers screamed "hot money." Two years ago a Los Angeles bank official noticed that Andonian Brothers Manufacturing Co., a jewelry broker, had made cash deposits totaling \$25 million over a three-month period. The suspicious banker alerted Federal agents. "I don't care how successful they are," he told them. "No one can sell that much jewelry in that little time."

That single tip, investigators say, led them to the biggest money-laundering case ever. They found ledgers in Andonian's trash bins showing that a mysterious "Raul" had delivered cash to the company. Agents in New York already were on the lookout for a money-laundering kingpin by the same name, who an informant said used jewelry stores to recycle drug money. In Atlanta, undercover agents of the Drug Enforcement Administration posing as money laun-

derers had learned of a Los Angeles group that could move large sums of cash offshore. The three probes quickly were linked.

The result: The breakup of a ring that allegedly laundered \$1.2 billion of drug money over two years, the Mar. 29 indictment of a respected Colombian bank, the arrest of 127 people, and the seizure of a ton of cocaine, some of it retrieved from New York City sewers. Officials believe they have penetrated the world's most powerful drug organization, the Colombian-based Medellín cocaine cartel. **'NEW ERA.'** As sweeping as the case was, its effects could go further. By indicting Banco de Occidente in Cali, Colombia, and seeking to force other banks where it had accounts to retrieve the money, the government is shifting strategies in the war on laundered drug money—some \$100 billion a year. "This signals

the start of a new era," declares Attorney Robert L. Barr Jr. of Atlanta, where the probe that led to the Colombian bank's indictment began. "We're striking at the heart of the [drug] financial infrastructure."

In fact, the case is not a fatal blow. But the indictment of Banco de Occidente, which did not comment by press time, is surely stirring up U.S. banks. For the first time, the Justice Dept. is using the civil forfeiture laws to force banks to return money they're holding in overseas branches. Chase Manhattan, Citibank, Bank of America, Marine Midland, and Barclays of Miami, among others, have been ordered to repatriate funds they are holding for Banco de Occidente in Panama and Colombia.

Justice, which wants to recoup a total of \$433 million, is also using a new legal theory. "We are saying that

A DAY IN THE



► Colombian cocaine is sold on Los Angeles streets. Proceeds of the sale are delivered by armored car to Ropex, a store in L.A.'s jewelry district. There, high-speed counting machines repack currency into boxes for armored car delivery to nearby banks.



► Once deposited, the funds are passed through several banks. A typical transaction involves a California bank accepting cash, then transferring the funds by wire to Ronel Refining Inc. account at Chase Manhattan Bank in New York. An unusual Chase then wires the funds to other banks; they wind up in a bank in Uruguay. The California bank also files the currency transaction report required by law.

y dollar [Banco de Occidente] took of the country, we can take an unre- dollar out of [its] net assets located e U.S.," says Charles Saphos, chief e Justice Dept.'s Narcotics & Dan- us Drugs Section.

at is going to extremes, argues a lay's executive. Five Banco de Occi- accounts at Barclay's were frozen ourt order. "I was surprised," he . "They are a very reputable, highly essional bank." By leaning on banks ft the confidentiality of foreigners' unt, government officials are "try- o scare the hell out of people," says ni tax attorney Robert E. Panoff.

COVER. Yet prosecutors may go further. The probe, code-named Op- on Polar Cap, could include the New : branch of Chicago's Continental t, which for five years has trans- ed funds for Banco de Occidente. eral agents searched the offices of inental's New York branch on Mar. According to a government affidavit in federal court in New York, a inental employee warned undercov- gents posing as money launderers they should have a legitimate com- as a cover. Law enforcement offi- refuse to comment on whether Con- tal is under investigation, while the : says that it does not believe it is insists that it turned away the ts.

aller banks, such as Guaranty In- tional Banking Corp. in Stamford, n., also transferred funds for Banco Occidente. Although many wealthy gniers send money to small banks, rment investigators want to know

if drug kingpins are using them as laun- dries. Guaranty International's lawyer denies any wrongdoing and says the bank cooperated with authorities.

Although banks fear losing business or breaking foreign bank-secrecy laws, "overall, banks are making a conscientious effort to comply with the law," says Salvatore R. Martoche, Assistant Treasury Secretary for enforcement. Investigators couldn't have broken this case without the banks' help.

The alleged money launderers— known as *La Mina*, or the Mine—dis-

SUSPICIOUS CASH

	Cash surpluses/deficits at local banks	
	1985	1988
	Millions of dollars	
MIAMI	\$6,000	\$4,500
LOS ANGELES	166	3,800
HELENA, MONT.	18	47
NEW YORK	-8,600	-11,000

DATA: FEDERAL RESERVE

guised their money laundering with gold-brokerage businesses, including Andonian, Ropex, and Ronel Refining, which service Los Angeles' jewelry district (diagram). The owners of all three were indicted and have since pleaded not guilty. Court documents show that Chase transferred \$307 million by wire to Banco de Occidente accounts. But investigators believe that Chase was an unwitting accomplice. Said a spokesman for Chase: "We are just a bystander."

The ring made substantial cash depos-

its, and the banks routinely filed curren- cy reports, which are required for depos- its of \$10,000 or more. But they raised few eyebrows because the gold business is cash-based. The ring also used wire transfers. U.S. banks each day move hundreds of billions by wire, yet such transfers need not be reported—an obvi- ous draw for launderers.

With wire transfers of \$23 billion a day at Continental alone, the cartel's transfers were tiny. But the original cash deposits were made in a city that the feds already were targeting. Since 1980, enforcement agencies have been closely scrutinizing the reports that each of the 37 Federal Reserve branch banks makes on currency movements in its re- gion. The data seemed to show Los An- geles awash in drug money (table).

The government probably won't get all the money back. Of the \$433 million that went to Banco de Occidente, only \$62.5 million has been frozen. The rest, investigators say, is supporting the lav- ish lifestyles of South American drug traffickers. But the gold brokers, jewel- ry stores, and other front companies that are said to have helped cleanse the money now are out of business.

Even the most gung-ho federal agents admit the money-laundering business is thriving. Banks may be cooperating un- der new pressure from the feds, yet bil- lions of drug dollars still seep into the system. But stay tuned. Federal officials say that when it comes to putting a chill on drug money, Operation Polar Cap is just the tip of the iceberg.

By Paula Dwyer in Washington and Pete Engardio in Miami

DRUG DOLLAR *As alleged in a U.S. grand jury indictment*



hile, false invoices billing fictitious clients for shipments of large amounts e sent between Ronel, a company that purports to be in the gold bullion and Ropex as cover for the wire transfers of funds between banks. To com- sham transaction, bars of lead coated with gold paint are shipped by Ronel which then sells the "gold" to other cooperating jewelry stores.



► In Uruguay, the funds are credited to the account of Letra, a concern that U.S. officials believe is controlled by the Medellín cocaine cartel. The Colombians then may repatriate their profits.

DATA: JUSTICE DEPT

Commentary/by William Glasgall and Vicky Cahan

QUESTIONS THAT KEEP SURFACING AFTER THE SPILL

Air transport is remarkably safe. Nonetheless, airports worldwide have teams on duty around the clock to rescue victims in case a crash occurs. To airlines and airports, the potential lifesaving benefits of such readiness far outweigh any costs. Oil companies led us to believe they were just as vigilant against spills. But as the wreck of the tanker Exxon Valdez showed, they weren't.

The 10 million gallons of crude spilled into Alaska's Prince William Sound have fouled beaches and fisheries and drawn charges and countercharges over who's responsible for the bungled cleanup. But however blame is apportioned, the slow response to containing the spill demonstrates something fundamental about the way oil companies perceive environmental risks. Worries Seattle oil consultant Arlon R. Tussing: "The system that was set up early on has disintegrated."

BIG BUCKS. The question is why. With the industry still slashing costs more than three years after crude prices collapsed, has the unglamorous job of investing in preventing and cleaning up such long shots as an oil spill been underfunded? Exxon Corp. says no. "How did we stack up? We did what we said we should do," insists Exxon President Lee R. Raymond.

Yet questions remain. Shouldn't Exxon and the Coast Guard, which licenses ships' officers, have maintained stricter controls over staffing the stricken tanker? The Exxon Valdez' captain, a former participant in a company-sponsored alcoholism-treatment program, was drunk and off the bridge when the tanker ran aground; at the helm was an unqualified third mate. And would it have made a difference if Exxon had heeded more than a decade of complaints by state environmental aides and insisted on more generous staffing and equipment outlays for the oil port it snafus? For an oil company as large as Exxon, heavily insured and with bil-

lions in unused borrowing power, is it simply cheaper to risk the occasional spill than to shore up its preparedness?

That's not to say the dollars involved in a cleanup aren't massive. No one knows how much it will cost to clean up after the Exxon Valdez. But oil-spill expert Richard S. Golob figures that cleaning up the 68 million-gallon Amoco Cadiz spill off Brittany in 1978 cost \$100 million. Add another \$117.5

William Sound that marks the southern end of the Trans-Alaska Pipeline, for mishaps have occurred. Just three years back the pipeline's operators—seven-company consortium including Exxon—even estimated that a spill of Exxon Valdez dimensions might happen only once in 241 years.

ASLEEP AT THE WHEEL. Trouble spills do happen. And there's some evidence that the industry is poorly prepared even for the medium-sized ones that have marred the Alaskan oil trade several times in recent years. In 1984, for example, a consortium that handles spills at Alaska's Cook Inlet wasn't up to the task when the tanker Glacier Bay leaked 125,000 gallons of crude. Similarly, the Alaska pipeline owners' group, which coordinates cleanup efforts around Valdez, was caught dozing when the Exxon Valdez began spewing its cargo. The cleanup team had flunked three "spill drills" in recent years. And its sole barge was laid up awaiting repairs. With no backup barge on standby, the crew lost 12 hours while loading equipment. Once the cleanup began, efforts were hampered by equipment shortages, a dispute between Exxon and the Coast Guard, and a debate over whether the team's contingency plan would work.

Even before the spill, the industry's environmental performance in Alaska was under fire. Now, Congress is likely to stall an industry campaign to drill in the Arctic National Wildlife Refuge. Lawmakers also may compel oil companies to set up a \$500 million fund for future cleanups. Some analysts believe the oil industry may head off such a move by revamping its plans to prevent and contain spills nationwide. That would be long overdue. But the industry can't be allowed to drag its feet any longer. A big spill might happen only occasionally. But a long time may pass before the damage from the latest one is fully erased.

VALDEZ' LEGACY: THE CLEANUP CREW TOOK 12 HOURS TO START



million in damages if a recent settlement recommendation stands. Big bucks all right, but still not much for any large oil company.

The industry's rhetoric—and to some extent the record—bolster the notion that complacency may have had much to do with the fiasco. Oil companies had gone to great lengths to convince the public that a major spill was highly unlikely. Indeed, though 250 billion gallons have been shipped since 1977 from Valdez, the port at the head of Prince

HY HUGH McCOLL IS COURTING ATLANTA BELLE

B's rough-and-ready chief wants Citizens' strong asset base

bold ex-Marine, NCNB Corp. Chairman Hugh L. McColl Jr. once declared that he wouldn't business down "every pig path in ia." What he long has hankered Atlanta's Peachtree Street, seat of cal elite. But McColl's rough-and- ways stymied many of his over- to the city's genteel bankers. In First Atlanta Corp. spurned him by dly accepting a lower offer from Wachovia Corp.

lettered, McColl is now courting tt A. Brown, the head of one of a's most venerable institutions, ns & Southern Corp. At the outset, a returned his calls but refused to wn for a meeting. Late on Mar. 30, Brown ignored McColl's ultima- NCNB launched a secret operation amed "Super Bowl," and at 9:57 nveiled a \$2.4 billion hostile bid for nd its \$21 billion in assets.

many, the assault was vintage ll: He sent NCNB staffers with per- letters to 10 C&S directors at home, g at least one from his

To woo C&S executives, CNB adviser says, McColl e would consider split- NCNB's headquarters be-

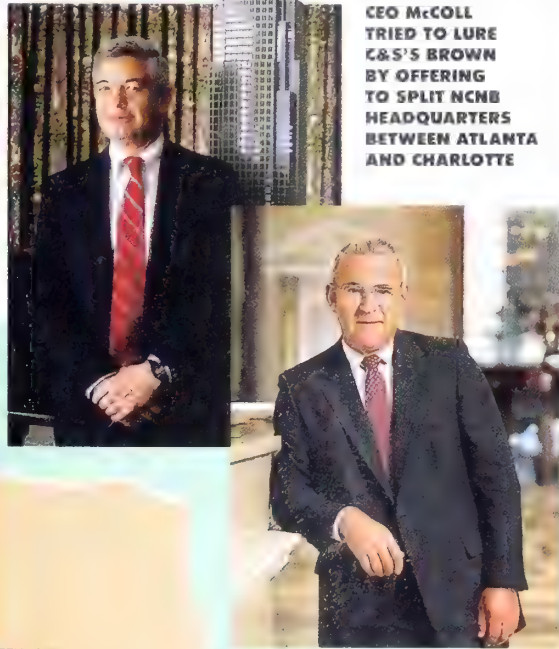
tween Charlotte and Atlanta and offer- ing Brown the NCNB chairmanship. But given McColl's track record of booting out management in other banks he has bought, those assurances surely aroused some skepticism.

The C&S board immediately rejected NCNB's bid. But McColl, 53, is the sort of fellow who can't hold back. Flush with respect from Wall Street since his dar- ing, bargain-price purchase late last year of failed First RepublicBank Corp. of Texas, he is driving to triple the assets NCNB manages to \$77 billion in just nine months. If he wins his war for C&S and finishes buying the 60% of First Repub- licBank in Dallas that NCNB doesn't own, McColl will head the sixth-largest U.S. bank—with the No. 1 presence in Texas, North and South Carolina, and Georgia and No. 3 in Florida (map). "There would be NCNB—and everyone else," says John

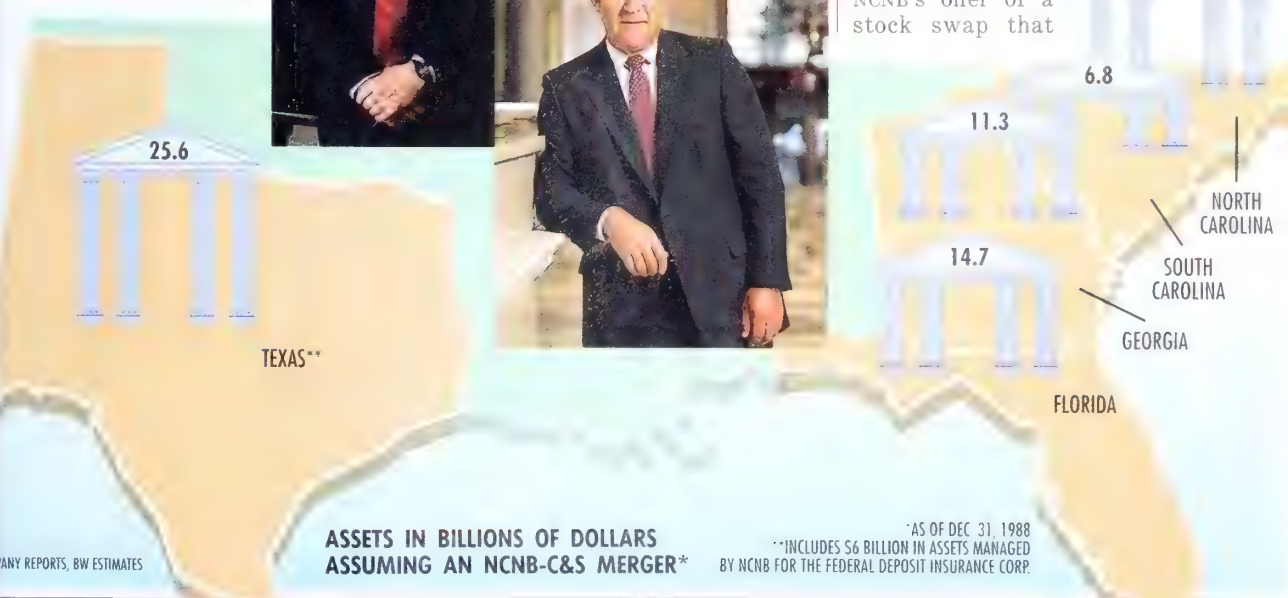
B. Moore Jr., principal with BEI Golembe, At- lanta consultants.

But McColl wants

CEO McCOLL TRIED TO LURE C&S'S BROWN BY OFFERING TO SPLIT NCNB HEADQUARTERS BETWEEN ATLANTA AND CHARLOTTE



IB'S MARCH ROUGH SOUTH



C&S for more than just size. He needs to tap the equity markets to pay for the remainder of First RepublicBank—with- out upsetting shareholders with a big dilution in equity. C&S's strong capital base—6.15% of average assets last year, compared with 5.74% for NCNB and 5.26% for the top 200 banks—would be a god- send. Just as important, C&S offers a source of cheap deposits for NCNB, whose rapid growth has kept it addicted to the high-cost money markets for funds. To retain deposits in the volatile Texas market, NCNB issues certificates of deposit with teaser rates as high as 15% for the first three months. C&S pays just 5.77% for funds, yielding a plump 4.78% net interest margin, compared with a 6.81% cost of funds that leaves NCNB with a margin of just 3.83%.

But McColl, who once let loose a fake hand grenade before staffers to see who would flinch, could find his high-stakes C&S bid blowing up in his face. He may not mind taking the risk: "You don't get your hands dirty with something this flamboyant if it can't be done," reasons the head of one Atlanta bank. Preserv- ing his reputation is the least concern. With NCNB under pressure to keep up its earnings momentum, McColl needs to make the most of what acquisition op- portunities remain in the Southeast.

'CLEARLY INADEQUATE.' On the other hand, NCNB's management ranks have been stretched by stepping into the Tex- as banking quagmire. And McColl's lat- est offensive comes at a time when some are questioning the frenetic acquisition pace of some superregionals. Analysts point to the indigestion at Charlotte's First Union Corp., which has gobbled up 21 banks in the past three years.

In any event, McColl has fired the first shot in what is shaping up as a classic South- ern feud. Despite NCNB's offer of a stock swap that

would give C&S shareholders stock worth \$39 a share, a sweet 46% premium over their shares' previous value, the Georgia bank quickly rejected McColl's offer as "clearly inadequate." Even though analysts say the company could fall at a bid in the mid-40s, McColl's offer, says C&S's outside attorney, H. Rodgin Cohen, "doesn't even come close."

C&S's best defense may come from federal and state regulators who must approve any deal. C&S intends to argue that NCNB's stock has soared 50%, to 36, since last summer, chiefly because of the favorable deal the regulators approved for its acquisition of First RepublicBank. It contends that NCNB is unfairly exploiting the government's aid in Texas to fund a hostile takeover. C&S advisers may recommend a stock buyback. Others predict a change in C&S bylaws that could discourage raiders by forcing them to shoulder hefty accounting charges for goodwill.

One former target, First Atlanta Corp.'s ex-Chairman Thomas R. Williams, believes the ultracompetitive McColl will return with a higher offer: "Hugh didn't fire his first and last bullet." McColl isn't talking, but history suggests he hates losing more than most folks. A third-generation banker from South Carolina, McColl was famous within his University of North Carolina fraternity for staging round-the-clock poker marathons that he usually won. "Money was never his motivation," recalls one frat brother, Dr. C. R. May III. "Making you quit first was." That trait persists. After crosstown rival First Union Corp. started work on the tallest building—42 stories—in downtown Charlotte, McColl responded with plans for his own 60-story tower, which locals nicknamed the "Taj McColl."

BIG LURE. While C&S derides McColl's all-stock offer as "speculative," institutional investors—who hold more than 40% of its stock—could be receptive to NCNB, whose prospects have brightened since it announced plans to acquire First RepublicBank. "The bait of what NCNB can do in Texas" is a powerful lure, says John J. Mason, McColl analyst for the Charlotte firm Interstate Johnson Lane.

Even if C&S somehow manages to escape, it's doubtful the Southern banking set will be able to ignore McColl. Already, he's bottom-fishing in Texas again, hoping to hook parts of another troubled Texas bank, MCorp. "We're trying to position ourselves to be one of the survivors when the shooting stops," McColl said a few weeks back. But nobody is promising he won't take a few prisoners first.

By Dean Foust and Scott Ticer in Atlanta, with Kevin Kelly in Dallas

RESTRUCTURINGS



CEO TELLEP: RAISING \$1.1 BILLION WITH SELL-OFFS "WILL ENHANCE OUR COMPETITIVENESS"

LOCKHEED DONS NEW ARMOR TO KEEP THE RAIDERS AT BAY

The defense contractor is selling more assets and creating an ESOP

It may prove to be the shortest long-term investment ever. On Apr. 3, Dallas financier Harold C. Simmons announced he had bought 5.3% of Lockheed Corp., saying he intended to stick around "for two to three years" to "get a real good return." Just two days later, after Lockheed unveiled a sweeping restructuring plan, Simmons announced that he had already sold off much of his 3.1 million shares.

For Simmons, the sales will likely just keep him even on his \$116 million investment. So Lockheed won't help him in the \$1 billion bid for another company he's said to be contemplating. He has asked the Federal Trade Commission for permission to buy stakes in Chrysler, Paccar, and Phelps Dodge worth more than \$15 million each.

But for Lockheed, the implications are far more profound. After more than two years of persistent takeover rumblings—and alleged suitors ranging from Ford Motor to Boeing—Lockheed finally seems to be getting serious about putting an end to all the talk. As Wolfgang H. Demisch, a defense industry analyst with UBS Securities Inc. in New York, puts it: "It's as if Lockheed is saying, 'enough is enough.'"

Over the past year,

Lockheed has unveiled similar, if sweeping, measures. In 1988, for instance, the Calabasas (Calif.) company sold off its profitable Dialog Information Services Inc. data-base services for \$353 million and finished buying back 10 million shares. But by late last year, its stock price had gained only 3½% and Lockheed still looked like real bait. Simmons began buying stock, accumulating a 0.6% stake in December. Rumor mills swirled anew.

PRIME PROPERTY. Now, following the ample set last year by Polaroid Corp., Lockheed is using an employee stock ownership plan to help it keep raiders at bay. On Apr. 4, the company issued \$1 million of new stock to a new ESOP, which gives the ESOP 17% of the company. Stake management says could increase substantially over the next 15 years.

To raise as much as \$1 billion, which the company will use toward acquisitions and a fresh stock buyback, the contractor will sell assets. Its profitable information systems group, which includes the Comp Group and CAI Inc., will be among the first to go. They will be followed by its 225-acre aeronautics plant in Burbank, Calif.—prime property that real estate brokers such as William R. ...



SIMMONS: HIS LONG-TERM STAKE WAS SHORT-LIVED

er of Cushman & Wakefield in dland Hills, Calif., say could go for o \$500 million. Lockheed CEO Daniel Pellep asserts that the moves "will nce our competitiveness."

ckheed could use the help. Along the restructuring, the company also osed that it expects its first-quarter ating profit to sink 40% below the million it earned in 1988. For the , the company projects operating ings to be off by 25% from the \$442 on it posted last year on \$10.6 billion enues. With higher revenues from roduction of the Trident missile and r research expenses, Lockheed ex- s profits next year to jump 20%,

Lawrence M. Harris, an analyst at man Eichler, Hill Richards Inc. e defense contractor's problems from the closeout of its \$6.6 billion ract to make C-5B cargo planes for Air Force. At its peak, the contract uted for \$2 billion in annual sales, 0% of Lockheed's total. But the last e will be delivered this month.

ckheed's problems don't end with C-5B, however. The contractor will complete its contract to supply the alled stealth fighter to the Air Force ell. With 77% of its overall budget ndent on the Pentagon, including r portions of the endangered State- fense Initiative, Lockheed is also ive to increasingly stringent federal ding limits. And while the company a \$5 billion contract to make anti- rine planes for the Navy, produc- isn't expected to begin until 1994.

PICS. Tellep predicts that the com- y will bounce back in 1990. It's look- to assemble MD-11s for McDonnell glas Corp. at its idled C-5B plant in ietta, Ga. The market for such es could be as much as \$5 billion a , according to Prudential-Bache Se- ties Inc. analyst Paul H. Nisbet. It is competing for the Air Force's Ad- ed Tactical Fighter, which could el as much as \$15 billion to the com- y over several years.

eanime, the measures are designed outress the stock price. But Wall et wasn't impressed: The stock sank ints, to close at 47¾ despite a nickel st in the quarterly dividend to 45¢ a e. "A lot of people have been con- ed all along that Lockheed would be n over," says Nisbet. "And this may e enough to convince the diehards." e reason: an estimated breakup value bout \$80 a share.

nothing else, the company has wn a strong will to avoid all those ored suitors. Still, it needs to make d this time on its latest restructur- or the next buyer may wait around tle longer than Harold Simmons.

y Eric Schine in Calabasas, Calif., with in Kelly in Dallas

THE B-2: CRUISE MISSILES
COULD DO THE JOB BETTER



Commentary/by Dave Griffiths

WHY THE STEALTH BOMBER SHOULD REALLY BECOME INVISIBLE

For more than a half-century, it has been an article of faith within the Air Force: Manned bombers capable of raining high explosives on factories and civilians can help win wars. That's no surprise when you realize that the steely-eyed young men who flew through clouds of flak over Germany and Japan became the generals who molded the modern Air Force.

The World War II commanders are long gone—but their philosophy lives on. That's why the Pentagon spent \$27 billion on the B-1B bomber, which has been plagued with troubles, and why it plans to purchase 132 B-2 stealth bombers at \$516 million apiece.

The manned bomber designed to penetrate enemy airspace is an anachronism. And its replacement is at hand. The same stealth technology that's supposed to make the B-2 nearly invisible to radar can be applied with even greater effect to the much smaller advanced cruise missile now being developed for the Air Force by General Dynamics Corp. By focusing its efforts on cruise missiles—which could be lofted from B-52s and B-1s—the Pentagon could save billions. And the Air Force could put into its arsenal a weapon that's just as effective a deterrent.

SLOW RECALL. The missiles would meet two key requirements set for bombers in the U.S. plan to prevent nuclear holocaust. First, the cruise missiles would provide insurance if the faster-acting missiles launched from silos on land and submarines at sea were somehow disabled or failed to work. More important, cruise-carrying aircraft, unlike ballistic missiles, could be recalled before they dispense their payloads. Although they don't allow as much time for recall as penetrating bombers, they still would allow a President to move to the brink while retaining the flexibility to respond to a Soviet at-

tack or pull back without firing a shot.

Some B-2 advocates contend that the U.S. still needs manned bombers in order to fight a war featuring multiple assaults and counterattacks. Only with a couple of pairs of eyes, they say, will there be any hope of spotting and destroying the mobile, land-based Soviet missiles that escape an initial barrage.

But that assumes that either side would keep fighting after a nuclear exchange. Says James P. Rubin of the Arms Control Assn.: "The basic issue with the B-2 is whether we want to spend almost \$70 billion to hit Soviet missiles after both countries have been irradiated and hundreds of millions of people may be dead."

MONEY WOES. Beyond the esoteric world of nuke vs. nuke, stopping the B-2 program well short of production could have some far-reaching side benefits. Much of the money saved could ease the pressures on the budget for conventional arms. Money problems are threatening to degrade combat readiness and force up weapons' unit costs by stretching out purchases.

Canceling the B-2 also would give the Bush Administration a chance to restore balance to strategic programs. As House Armed Services Committee Chairman Les Aspin (D-Wis.) points out, a huge 60% of the \$215 billion that the Reagan Administration spent on nuclear weapons systems went to bomber programs. Only 16% was devoted to land-based missiles, which, both Democrats and Republicans agree, are still the most vulnerable to being knocked out by a surprise attack.

There are signs that common sense may triumph. The Pentagon may delay the B-2 program beyond 1991, when the first delivery is planned. Instead, it should dump the stealth bomber altogether. The days of *Thirty Seconds over Tokyo* are gone forever.

SMITHKLINE THINKS BEECHAM CAN CURE WHAT AILS IT

And mergers look like the Rx to many drugmakers with global ambitions

Tagamet, the ulcer medicine that turned SmithKline Beckman Corp. into a high-flying drug company in the late 1970s, was developed in the company's British research labs. So it's fitting enough that Chairman Henry Wendt is looking to Britain again now that SKB needs some more strong medicine. On Apr. 2 the company confirmed that it's holding merger talks with Britain's Beecham Group PLC.

The alliance would form one of the world's biggest prescription and over-the-counter drug companies. Beecham, already potent in OTC drugs and consumer products, wants to boost its stateside presence in prescription medicines. SKB would give it a big U.S. pharmaceutical research and sales arm. For its part, SmithKline may need a merger to quell takeover fears. And it could use Beecham's marketing clout when it reformulates Tagamet for over-the-counter sales.

RIVAL SHOPPERS. The synergies may seem obvious, but the deal is far from done. For one thing, it's not clear how Beecham's chairman, Robert P. Bauman, 58, and Wendt, 55, would mesh. The companies couldn't even agree on a proposed modest joint venture some years ago. And a 3¼-point runup in SKB's stock by Apr. 5 suggests that investors expect other bidders. Analysts say players such as Switzerland's F. Hoffmann-La Roche & Co. are too eager to crack the U.S. market to let this deal go through uncontested. Other companies that may be looking to step up their U.S. presence include Britain's Imperial Chemical Industries, France's Rhône-Poulenc, and Japanese drug companies. Possible American contenders include Pfizer Inc. and Du Pont Co.

Beecham itself could draw a bidder's interest. The company's stock rose 4.2% the day after disclosure of the talks. "Beecham management has accepted that the company can't make it on its own in the 1990s and is implicitly invit-

ing hostile offers," says an analyst at S. G. Warburg & Co. in London.

Whatever the fate of this deal, it's not likely to be the last. The drug industry is heading for a period of worldwide consolidation. Pharmaceutical companies need vast research and development budgets to finance the steep costs of creating new drugs, and they need worldwide sales to recoup that expense.



SKB'S WENDT AND BEECHAM'S BAUMAN: DO THEY NEED EACH OTHER?

A NEW GIANT IN THE MEDICINE CHEST?

Pharmaceuticals	Consumer products	Over-the-counter
SMITHKLINE BECKMAN		
▶ TAGAMET (ulcer treatment)	—	CONTAC
▶ DYAZIDE (antihypertensive)	—	ECOTRIN
BEECHAM GROUP		
▶ AUGMENTIN (antibiotic)	AQUAFRESH	GERITOL
▶ AMOXIL (antibiotic)	BRYLCREEM	TUMS
▶ EMINASE (heart attack treatment)	—	SUCRETS

DATA BW

Besides mergers, many companies are swapping products or signing deals to sell one another's drugs. And some companies are hooking up with consumer marketers, hoping to extend the life of their aging prescription drugs by taking them OTC.

Internal documents prepared for the merger and obtained by BUSINESS WEEK make it clear that such competitive worries played a major role in the proposed SKB-Beecham deal: "Virtually all firms are seeking marketing partners to ex-

pand their penetration," the documents note. Among such alliances already formed are Glaxo and Roche, Upjohn and Beecham, Squibb and Johnson & Johnson, and J&J and Merck. The merger papers argue that Beecham alone couldn't easily rise from a worldwide rank of about No. 23 in prescription sales, while a stand-alone SKB might be hard-pressed to "hold its current position" at about No. 6.

That's because SKB has been having its troubles. Generic rivals knocked its Dyazide blood-pressure medication sales to about \$200 million in 1988 from some \$350 million the year before. And Tagamet's market share fell from 58% in 1986 to an estimated 30% under pressure from Zantac, an ulcer medicine from Britain's Glaxo Holdings PLC. With

new drugs coming out in the past few years, SKB had nothing to fall back on. "SmithKline spent a lot of money on research, and they haven't produced the goodies," says David Peters, a director of Fisons PLC, a \$1.3 billion British pharmaceutical house. After big restructuring costs for layoffs, SKB's pretax profits plunged 62% to \$308.4 million, on a sales increase of 9.7%, to \$4.8 billion.

SOOTHING BALM. Beecham, meanwhile, has prospered. Robert P. Bauman, an American veteran of General Foods and Textron who joined Beecham in 1986, shook up management and pruned lines such as soft drinks. The payoff: Pretax profits rose 15.4% in the year ended in March, 1988, to \$85 million, even as sales rose 10.4%, to \$4.2 billion.

But Bauman needs the U.S. market to hit his goal of boosting earnings-per-share growth to 20% from last year's 16.3%. Beecham has a number of new drugs that could do well in the U.S., especially if they're sold by SKB's sales force. These include Eminase, a clot-dissolving

treatment for heart-attack victims, and Relifex, an arthritis remedy.

The Beecham-SKB deal could be soothing balm for shareholders, too. SKB's stock is showing its first signs of life in months. And Beecham's stockholders may profit from a plunge into the U.S. But the big payoff may be yet to come. A global takeover battle in the drug industry would be the sort of medicine shareholders could happily swallow.

By Joseph Weber in Philadelphia and Mark Maremont in London



CILMAN CRAMER IS OUT TO SPUR RECYCLING—AND TOUGHEN STATE AND FEDERAL LAWS

WORD OF ADVICE, BENJAMIN: LAY OUT OF PLASTICS

you're being restricted in Minneapolis—and threatened elsewhere

How's this for effective lobbying: Fearing that a tough proposal to ban nonrecyclable plastic at food stores and restaurants might squeak through the Minneapolis City Council, the plastics industry and local grocers lobbied the city with radio and newspaper ads urging residents to phone City Council members in opposition. People called in, all right—but they overwhelmingly favored banning plastic packaging. "I got more calls on this than any ordinance we've ever considered, whether cat-leashing or dog licensing," marvels one council member. As a result, on Mar. 31, instead of the expected close vote, the ordinance passed by a 12-0 vote.

The ban, considered the nation's most stringent, has the food and plastics industries plenty worried. What really terrifies them, though, is the thought that the backlash in Minneapolis portends a growing national sentiment. Joel R. Hoi, a spokesman for the Minnesota Plastics Assn., frets that "people really have a distaste for plastic."

LANDFILLS. Most plastic isn't biodegradable. And it's taking up an increasingly large share of the nation's garbage: The Environmental Protection Agency expects it to hit 8% by the year 2000, up from 3.5% in 1975. Landfill space is short, particularly in the Northeast, so local governments are seeking ways to trim their trash. Recycling is on the rise. Many programs are becoming

mandatory: A New York City effort, which goes into effect this summer, carries fines of up to \$500 for those who don't separate recyclable trash. Statewide recycling programs are set to go into effect in New Jersey, Florida, and seven other states in the early 1990s.

Lobbyists for plastics manufacturers acknowledge the solid waste problem and say they stand foursquare behind recycling. But they bridle at the bans on specific materials that are beginning to pop up around the country. Beginning in July, Styrofoam and other polystyrene plastics will be banned at fast-food restaurants in Suffolk County, N.Y. As much in reaction to threats to the ozone layer from polystyrene manufacturing as to solid waste problems, similar restrictions have been passed in Berkeley, Calif., and Portland, Ore.

The Minneapolis ban is far broader in scope. Set to begin in July, 1990, it would prohibit all food packaging at grocery stores and restaurants that is not biodegradable, returnable, or collectible

Beginning this summer, New Yorkers must separate recyclable goods from their trash—or face a \$500 fine

for recycling. But it's unclear just how much plastic packaging would actually be banned. The city plans to add plastics to its existing recycling program, so milk jugs, soft-drink bottles, and other recyclable plastics would be allowed. Wrappings for products such as meat and bread are exempted.

At this point, determining what products would actually be banned is anybody's guess, thanks to a huge loophole in the law: The ban doesn't cover environmentally unacceptable packaging "for which there is no commercially available alternative." The city's health commissioner, with help from an advisory board, will decide which products qualify for exemption. The board will be allowed to consider "competitive effects" in its decision-making. "They'll be looking at thousands of products," says Roger D. Bernstein of the Council for Solid Waste Solutions, a plastics-industry lobbying group. "We think it would take a Pentagon-sized bureaucracy to deal with this."

DUBIOUS MOTIVES? If the local bans spread, manufacturers and distributors fear they'll face a chaotic patchwork of differing regulations. The author of the packaging ban, Minneapolis City Councilman Steve Cramer, says he would rather see the state or federal government take action. But he questions the motives of some of those pushing uniformity in packaging laws. "Many people would view uniformity as no action at all," he says. The primary objective of his ordinance is to spur recycling, he says, and he hopes that local bans will goad state legislatures and Congress into action.

Some plastic manufacturers, eager to preempt activists who want to ban their products, are already pushing recycling. Dow Chemical Co., which makes Styrofoam, is pumping more than \$1 million into a plastics recycling program in Akron, Ohio. Procter & Gamble Co., which says its products account for 1% of all solid waste in the U.S., is trying to create markets for secondhand plastic by using it in its own goods. Recently it began selling the liquid version of its Spic and Span cleaner in recycled plastic bottles.

Meanwhile, Bernstein's industry group is working to overturn the Minneapolis ordinance. A suit is expected that would challenge the ban as an unconstitutional restraint on interstate commerce. And the Minnesota legislature is considering a measure that would bar local governments from enforcing such rules. Whatever happens, it's clear that the public's desire for convenience is clashing head-on with the goal of a cleaner environment.

By Russell Mitchell in Minneapolis, with bureau reports

MILKEN'S SHADOW HOVERS OVER FRED CARR

First Executive's chief belonged to the junk-bond king's financial circle

On the eve of the Apr. 5 Predators' Ball, Fred Carr wouldn't say whether he was taking his tuxedo out of mothballs. Little wonder: The chairman of First Executive Corp. has been a frequent guest at Drexel Burnham Lambert Inc.'s legendary Beverly Hills gathering of junk-bond market players. Now, with Drexel junk king Michael R. Milken facing a 98-count federal indictment for securities crimes, it's natural that Carr might reconsider the company he keeps.

Inclusion in Milken's inner circle of junk-bond buyers helped Carr build First Executive into the nation's 15th-largest insurer. But the link has also brought Carr unwanted notoriety that ties his name to the various federal probes of Drexel. Worse, it has hurt both First Executive's sales and its stock price, while prompting concern among investors and customers. Question: Has Carr worn out his welcome? "There's a great sense of an image of impropriety," says one New York investor. "It may not be his fault, but as a shareholder, it's killing me." Lon Morton, a Calabasas (Calif.) insurance agent who sells the company's policies, adds: "There have been a lot of agents reluctant to do business with First Executive."

'MIND-BOGGLING.' Carr's soaring profits and cash flow, while Carr is engineering a boom in profits and cash flow. By cutting

costs, he has squeezed more profit out of his California and New York units, the company's two largest. In 1987, First Executive earned \$177.8 million on revenues of \$3.5 billion. Last year, while revenues sank to \$3 billion, net jumped up to \$204.5 million. And the future looks bright. "He's going to earn so much money it's mind-boggling," says John LaFrere of Delta Capital Management, which holds about 4% of the stock.

Despite all that good news, Milken's shadow hovers over Carr. It grew darker on Apr. 3, when Columbia Savings & Loan, another key member of Milken's network, said that it gave the feds rec-

ords of its Drexel trades. Carr, who in an interview wouldn't say whether he has done likewise, has helped Milken finance deals by buying bonds of many Milken clients, including Revlon, Texas Air, and Wickes.

What's more, Congress has been looking into Carr's role in Houston financier Charles E. Hurwitz' 1985 takeover of Pacific Lumber Co. A House committee is



Carr's notoriety has drawn attention away from the boom in profits he has engineered

probing allegations that First Executive improperly won a \$37 million contract for annuities to cover PL employees whose pension plan was raided to help finance the buyout. First Executive bought \$70 million of the bonds Hurwitz floated in the takeover. Carr, who is co-operating in the probe, calls the charges "inaccurate." The committee has referred the matter to the Labor Dept.

But it's the Carr-Milken connection that's in the spotlight. Milken, who raised capital for First Executive, has stock in two companies in which First Executive was a major shareholder: Regency Equities Corp., a Nebraska insurer, and First Stratford Inc., a California reinsurer. Earlier this year, the federal grand jury probing Drexel subpoenaed Regency Equities' records.

Although Carr now deals with junk-bond underwriters, his continuing heavy reliance on junk, which makes up 51% of his \$17 billion portfolio, is causing him problems in New York. State regulators insist that insurers limit junk-bond holdings to 20% of investments. In 1987 they forced First Executive to provide \$151.5 million in fresh capital for the New York unit.

The company is still trying to sell a subsidiary, which analysts estimate as Legg Mason Wood Ward Inc.'s David E. Nelson told Carr he could fetch \$500 million or more. **CASH COWS.** Carr scoffs at the idea who foresees a collapse in junk bonds in a recession. "If you're careful in your judgments of the credits that you buy," he says, "you're going to do O.K." Carr's side is First Executive's great financial strength: Debt is low and expenses are lean. In 1987, Capital's LaFrere applauds Carr's cutback of annuity sales. "Once you slow these companies down, they become cash cows."

But will Carr be around to see the land of milk and honey? The happy shareholders have put two proposals to aid the stock on the ballot for First Executive's annual meeting in June. Shareholders are potentially a powerful force, a mere handful of investors including Peter Lynch, manager of Fidelity's huge Magellan fund (page 68), John M. Templeton, and Rosewood Financial Partners, controlled by a trust of heiress Caroline Hunt, now worth about half the stock.

Indeed, it has become a source of the Wall Street rumor mill that Rosewood Financial, or the Louisville-based insurer ICH, which already owns 20.1%

First Executive, might bid for the company. More intriguingly, Carr might take the company private. With stock now trading at around 15%, a buyout would cost at least \$1.4 billion. But that way, he wouldn't have to wait what the rest of the world thinks of it.

By Kathleen Kerwin in Los Angeles with Christopher Farrell in New York and Tim Smart in Washington

“What my little company needs
is the kind of computer only
a big company can afford.”



IT'S A DIRTY JOB—BUT A LOT OF PEOPLE WANT TO DO IT

New York's mayoral race is already getting crowded—and heated

Although the New York mayoral race is still two months off, the competition has already begun in earnest. On Apr. 8, New York's small Liberal Party is set to endorse Republican Rudolph W. Giuliani, the former U.S. Attorney who gained fame prosecuting organized crime and World War II veterans.

Liberal backing boosts Giuliani's drive to round up a big chunk of the city's 2 million registered Democrats, who outnumber Republicans by about 5 to 1. He's betting that party stalwarts who normally wouldn't dream of voting Republican will cross the shorter ideological span onto Liberal turf. Giuliani's only GOP opposition is Ronald Lauder.



All these hopefuls are pursuing a prize that the U.S. Supreme Court just made more tantalizing. On Mar. 23 the court declared the city's fiscal body, the Board of Estimate, unconstitutional—because its composition denied the city's more populous boroughs voting power commensurate with their size. Most observers expect that a more representative form of government will enhance mayoral powers.

Koch's biggest vulnerability is the degree of



MANHATTAN BOROUGH PRESIDENT DINKINS (LEFT) IS LIKELY TO BE THE MAIN DEMOCRATIC CHALLENGER. BUT KOCH'S BIGGEST THREAT TO A FOURTH TERM COMES FROM FORMER U. S. ATTORNEY GIULIANI

votes. He's likely to argue that Giuliani lacks the experience needed to run a city and point out that some of the former prosecutor's splashiest cases, such as the one alleging Mafia control of Fulton Fish Market, met with failure.

Most polls give the mayor about 40% of the city's Democratic vote. He needs at least 40% in the primary to avoid runoff. Dinkins starts with a base of similar size, concentrated among black and white Manhattan liberals. The tough president, who is black, needs to extend his reach into the white ethnic enclaves of New York's four other boroughs. And while voters there are growing disenchanted with the mayor, many will vote for Ed Koch before the vote for a black person," says Robert Pecorella, an associate professor of government at St. John's University.

CROSSING LINES. Hispanics, who make up about 15% of the city's electorate, could swing the race either way. They're also the kind of socially conservative Democratic voters who may become Giuliani's messiah. Giuliani is positioning himself as an outsider with



former Ambassador to Austria and heir to the Estée Lauder cosmetics fortune, who is given little chance of winning.

Giuliani, Lauder, and at least four other candidates make up the field in what promises to be the most competitive mayoral contest since Edward I. Koch first won election in 1977. To capture an unprecedented fourth term, Koch first must beat back challenges from fellow Democrats David Dinkins, the Manhattan borough president, City Comptroller Harrison J. Goldin, and Richard Ravitch, a political novice who once ran the city's mass transit system. If Koch beats them in the Sept. 12 primary, as is likely, chances are he'll face Giuliani, who is expected to declare his candidacy in late April or early May.

blame voters assign him for the city's widespread problems. Corruption scandals have riddled his administration, homeless people bed down along Fifth Avenue, and crack dealers ply their trade openly on the streets. Murders in the city hit a record 1,915 in 1988.

MIGHTY MOUTH. The mayor's rivals, led by Dinkins, say that Koch can no longer address New York's problems, and that his rhetoric has divided a city in need of reconciliation. Even Koch's media adviser, David Garth, says the mayor "doesn't keep his mouth shut" when it would be wise to do so.

But the force of the attacks on Koch are evidence that no one counts him out. He's a slashing campaigner who will court controversy if he thinks it can win

wherever to revive the city. "The present mayor," he says, "has exhausted his ability to do new things and to take on problems."

Giuliani is also crossing party lines to recruit his staff. According to sources familiar with the campaign's workings, he'll probably hire a Democratic media consultant to team with top GOP pollster Robert M. Teeter.

The Giuliani organization had been ready for a bruising fight. Although Koch looks vulnerable, his challenger will have a hard time unseating him. "A feisty mayor," says Garth, "can do anything anybody crazy, including me." But he may be just the kind of mayor a boisterous town like New York wants.

By Harris Cole

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EDITED BY HARRIS COLLINGWOOD

RUDERMAN IS SENTENCED

► S. G. "Rudy" Ruderman was no big-fish inside trader like Dennis Levine or Ivan Boesky. But he, too, is going to jail.

After a long, unblemished career, most recently as BUSINESS WEEK's radio broadcaster, Ruderman, 62, began trading small lots of securities in 1986 using advance knowledge of BW's "Inside Wall Street" column. On Dec. 9 he pleaded guilty to two counts of mail fraud, and on Apr. 5 he was sentenced to six months in prison and three years' probation. He also was fined \$5,000. The judge, who could have sent the former broadcaster away for 10 years and extracted \$100,000 in fines, said he had taken Ruderman's history of heart trouble into consideration.

CONRAIL MAKES ANOTHER STOP AT CSX

► For the second time in recent years, Conrail has raided CSX for a chairman and chief executive. James Hagen, 57, on May 18 will succeed Richard Sanborn, who died of a heart attack on Feb. 12. Hagen took Sanborn's post as head of CSX Distribution Services group when Sanborn joined Conrail last year.

Hagen will continue Sanborn's drive for customer service improvements and explore new businesses for Conrail. Hagen was senior vice-president for marketing and sales at Conrail from 1977 to 1985. He earlier headed the government agency that helped form Conrail.

PEROT'S DETOUR INTO DATA PROCESSING

► Perot Systems, the startup venture of Dallas billionaire Ross Perot, is changing direction. On Mar. 30, Perot Systems formed a data process-

ing company with ICH, the big insurer. The agreement, which gives 50% ownership to each company, calls on Perot Systems to consolidate and upgrade ICH's data processing facilities. ICH will contribute \$36 million to the project, as well as computer equipment and 600 employees.

The move is a strategic shift for Perot. Last June, when the former head of Electronic Data Systems unveiled his company, he committed to undertaking only highly complex computer installation projects. Now that he owns a data center, Perot plans to chase traditional batch-processing jobs. Look for new competition between Perot and EDS for that sort of work. This could further sour already strained relations between the companies.

PICKENS PLIES HIS TRADE IN JAPAN

► Can a U. S. corporate raider find happiness overseas? Boone Pickens has bought a 20.2% stake in Japan's Koito Manufacturing. He's now Koito's largest shareholder, with an investment valued at \$1.2 billion. Koito makes automotive lighting products for the likes of Toyota, which is Koito's second-largest shareholder with 19% of the company. The Texan also says he's looking at other Japanese invest-

THE FDA IS A SUCKER FOR MEDICINAL LOLLIPOP

Surely you can still see your mother's furrowed brow as she handed you a chewable aspirin or your daily vitamin. "Remember, dear, this is not candy, it's medicine." The Food & Drug Administration should have known better than to buck the collective wisdom of millions of moms. But it did, and now it has a live one on its hands.

More than three years ago, the FDA approved the testing of lollipops laced with fentanyl, a potent and addictive pain reliever. The suckers are made by Anesta, which hopes to win approval soon to sell them. They're given to children about to undergo painful hospital procedures. But the Washington-based Health Research Group, a Rand Nader affiliate, is campaigning to block approval, arguing that nationwide marketing could lead kids to associate medicine with candy. Anesta and the FDA are responding that tighter controls will keep that from happening.

ments, although he declines to be more specific.

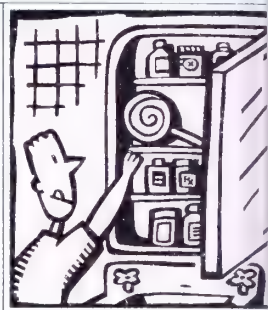
Countering rumors circulating in the Japanese market, Pickens insists he's not plotting a takeover—or a greenmail grab. Tokyo traders seem to believe him: Koito stock dropped slightly following Pickens' announcement.

PSNH: GOING, GOING, GONE?

► The bids are in, finally, for bankrupt Public Service of New Hampshire. On Apr. 5, New England Electric System offered \$1.4 billion in cash

and stock for the utility's generating assets, topping \$200 million in all-cash offers from Northeast Utilities. Neither acquirer is willing to touch PSNH's 35% stake in long-idle Seabrook nuclear power plant.

A takeover won't bail out PSNH shareholders. Duff Phelps analyst Thomas Hamlin reckons that under either offer, PSNH would have just \$300 million left after paying off bankruptcy expenses and holders of mortgage debt. And it probably would recapitalize equity to unsecured creditors. That, Hamlin says, "doesn't leave \$4 a share, which is about where PS stock has traded recently."



A RETAILER GOES ON THE RACKS

► Retailer Carson Pirie Scott is on the sale rack. On Apr. 5, P. A. Bergner launched a \$1-a-share offer for Carson, which owns 33 department stores in the Midwest. Bergner, which is wholly owned by the Maus and Norman retailing families of Switzerland, says it's willing to buy Carson's department store business or possibly the whole company. Carson is mulling over the offer.



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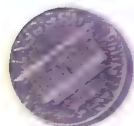
For 61 cents a day, here's what GTE's new



You'll have the satisfaction of getting more features—there are 13 in GTE's CentraNet 1000 package—at less cost than ever before.



You'll have an advanced, highly efficient business communications system, without having switching equipment on your premises.



Each month, you'll be able to check how much each station's phone calls cost you.



Thanks to individual station billing, you'll be able to ask the new employee about all those calls to New York—at your expense.



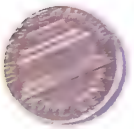
24 hours a day, 365 days a year, GTE's computerized, self-diagnostic systems will work to keep things running smoothly.



If something should go wrong, the chances are we'll have it fixed before you even notice it.



You'll be able to tell by the sound of the ring whether a call is coming from across the hall or across the country.



You'll have a business phone system that can grow with you: GTE's CentraNet 2000 and 3000 packages offer even more sophisticated features.



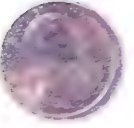
Your communications will have the quality you'd expect from GTE's advanced network.



GTE's CentraNet service means that you'll be able to schedule changes months in advance, or as soon as this morning.



If the lights should go out, your telephone service will stay on.



When Burt in Bakersfield won't get off the phone, that important call from Encino will go automatically to your secretary.



Your speed dialing feature will remember the eight numbers you call most often.



You may be able to beat someone to the best table at Mario's, because you only have to punch in two numbers, not the usual seven.



GTE's CentraNet service will turn the ordinary touchtone phones you already own into highly sophisticated business tools.



Your small branch offices will be able to have the same telephone features as your big home office.



You may be able to breathe new life into your aging key system, without having to buy yet more expensive equipment.



If Deborah needs a phone that has all the features, you'll be able to give it to her without having to give the same features to John, Linda, Michael and Melissa.



You'll be able to add lines by making just one phone call to a GTE Account Executive.



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You'll probably pay less for your fire theft insurance, since you won't have to buy costly switching equipment to insure.



You may be able to catch Doug before he leaves for lunch, because like everyone else, he'll have his own direct line.



If you land a big contract, CentraNet will offer more than congratulations: our optional features range from 8-party conferencing to automatic call distribution.



You'll be able to answer the phone in your partner's office without even leaving your own.

CentraNet[®] can do for your business phone.



You'll see a lot less of your phone repairer, since the switching equipment is monitored and maintained on GTE's premises, not yours.



You'll probably be able to tear up that oh-so-expensive service contract.



You'll have an extra office or storeroom, instead of a room that's packed full of telecommunications equipment.



You'll be able to impress your business associates with "Excuse me, I have another call on this line." (They'll be even *more* impressed if they happen to be the other call.)



Your company can expect to save a bundle in trunk charges. There aren't any.



Your switching equipment isn't going to need air conditioning in summer (remember, you don't have any switching equipment).



Your switching equipment isn't going to need heating in winter (ditto).



CentraNet can save a business with 160 lines \$51,450 in five years, compared to a PBX system. (Ask your GTE Account Executive to explain the assumptions behind these numbers.)



You'll be able to transfer calls without needing a master's degree in telecommunications.



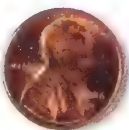
You'll have the most advanced business phone system of 1989. And 1990, 1991, 1992... the point is, as soon as we get new technology, so do you.



You'll only need to hit four numbers, to find out what's going on in the Sacramento office.



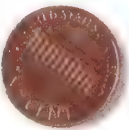
Thanks to direct inward dialing, every call doesn't have to go through your receptionist. So there'll be more time to help your customers who really need it.



If you're an accountant, you'll be able to cope with the usual overload in April, without having spare capacity in September.



Same for ski operators after the first snowfall, fireworks manufacturers on the Fourth, florists' shops on Valentine's Day.



You can change your mind about the features you need, and not have to change \$20,000 worth of equipment.



Installation won't mean weeks of hassle and headaches. If the wiring's already in place, all it often takes is a phone call.



With CentraNet's station hunting feature, incoming calls can be automatically routed to ring phones that aren't busy.



You can find out who in your company uses which features, when and how often.



You'll be able to invest the capital you don't spend on phone equipment on something else that your business really needs.



You'll be able to brainstorm with Jack (in Detroit) and Jacqueline (in Delaware) simultaneously, thanks to 3-way conferencing.



When you're talking to Ed, and Bill calls, you can answer him, buzz Brian, tell Bill what Brian said, then get back to Ed.



You'll sound like a million dollar corporation, even if you're just a two-person company.



We could go on, but it might be better to call 1-800-325-6844, and speak to a GTE Account Executive. Just say you'd like their two cents' worth on what CentraNet can do for you.

GTE

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We're not so
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Recently we've been letting big business know just how big a real estate firm we've become.

But how we got so big is a big reputation for service.

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Are you looking for a small space out in the wide open spaces? Call your local Grubb & Ellis office or our national toll-free number, 1-800-635-9860, for all your real estate needs.

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SPACE TECHNOLOGY. THIS IS WHAT'S IN IT FOR YOU.

The end of the terror message

Each one of these PC screens is saying something different. But they're all telling you the same thing.

You and your data are in a whole lot of trouble.

Perhaps someone hit the wrong key and deleted your data by accident.

Perhaps it's simply lost somewhere on your disk.

Or perhaps the disk is corrupted and everything is lost.



The Standard Edition gives you UnErase, File Find and a range of features, functions and enhancements — at an even more reasonable price.

Perhaps you should get the new Norton Utilities®.

Because only the Norton Utilities can take the terror out of all these error messages.

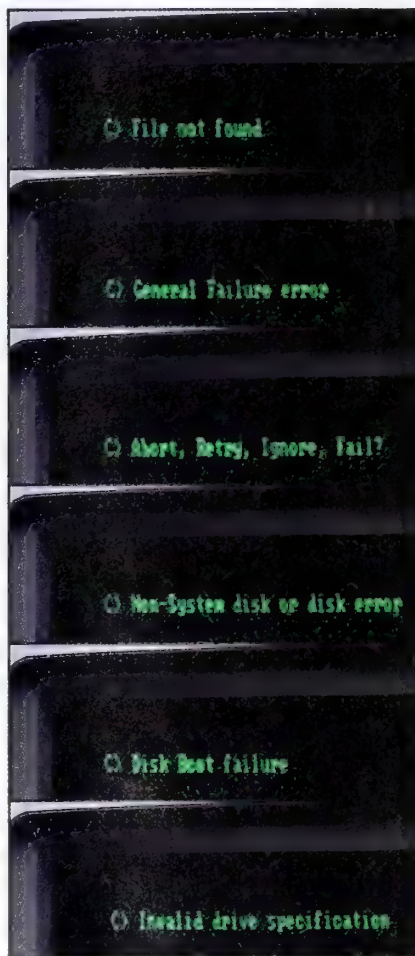
If someone has accidentally

deleted your data, fear not. Our legendary *UnErase*® can resurrect it with a few simple keystrokes.

If you've misplaced it — which, when you're dealing with a hard disk, is terrifyingly easy to do — our *File Find* will come to the rescue.

And what if worse comes to worst and your whole disk goes down?

Cheer up.



The extraordinary new *Norton Disk Doctor*™ will determine the exact nature of the problem, report it and, in most cases, fix it for you.

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In which case, you'll need to refer to *The Norton Trouble-*

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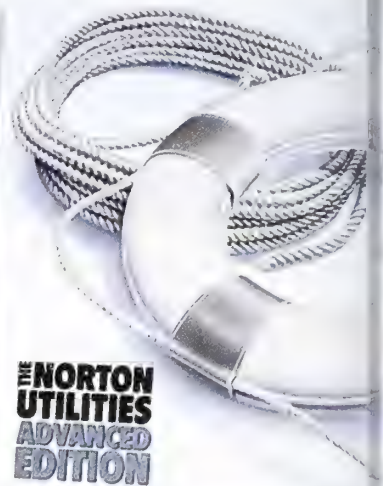
Don't worry, you don't have to go to the library or the bookstore to refer to it, because it's included in the Advanced Edition.

Along with 24 more organizational and disk management utilities we don't have space to mention.

PC Magazine calls the Norton Utilities "indispensable."

You'll want to call your local software dealer. Or call us at 1-800-365-1010.

Then you'll have nothing to fear but fear itself.



Peter Norton
COMPUTING

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On the front line. And on the production line.

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Now we are helping to build one more. By making a grant to help restore one of our original B-24s to its original condition. Soon a B-24 Liberator, which first flew in the Pacific, will fly again, this time in air shows around the USA.

Not as a symbol of American military might. Or of American manufacturing muscle. But of the American spirit which makes them both possible.

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A Strong Company For A Strong Country

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LEE ATWATER'S GOP OFFENSIVE GOING OFF AND STUMBLING

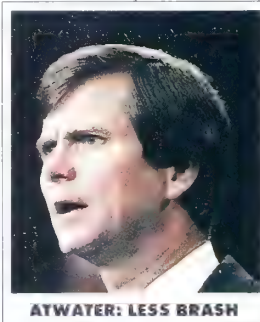
As the old saying goes, you have to suffer if you want to sing the blues. Just ask Lee Atwater, 38, hero of George Bush's election triumph, youngest-ever Republican Party chairman, and devoted blues guitarist. In the heady days after the election, Atwater was the hot act in town. He stormed the Republican National Committee, vowing to turn it into an aggressive political machine that would make the Republicans the majority party by the end of the century. He recruited such Republican heavyweights as Howard J. Rollins Jr. to lead an assault on Democratic control of the House. And Atwater launched a high-profile campaign to woo black voters to the GOP.

But a string of political reversals is showing how tough a time Atwater's ambitious agendas faces. In an Apr. 4 special congressional election that the Republicans had hoped would demonstrate the party's growing appeal in the South, a Democrat prevailed. Alabama Secretary of State Glen Browder routed state Senator John Atwater, a onetime Democrat. The lesson: Southern love of Republican Presidential candidates doesn't carry over to other offices. "The South isn't going to be converted in a day," says John Atwater, chairman of the National Republican Congressional Committee.

'MILIATION TIME.' An Indiana election proved even more embarrassing when a Democrat won the House seat once held by Representative Dan Quayle. Republican Daniel R. Coats, who was appointed to serve out Quayle's Senate term, won more than 60% of the vote in the district last fall. But on Mar. 28, Democrat Daniel G. Heath lost to Jill Long, whom he had tried to label as a "Dukakis liberal." Republican officials now concede they erred by trying to nationalize the campaign. Long focused on her record of opposition to local taxes. These defeats have raised the stakes in Wyoming, where Republicans are battling to hold the House seat vacated by Defense Secretary Richard B. Cheney. Democrat John Vinich, who ran a strong race against Senator Malcolm Wallop last year, is favored. "I expect them to throw everything they've

got into it," says Geoffrey Garin, Vinich's pollster. "If they end up losing all three special elections, it's humiliation time for the Republicans." Grouses one GOP strategist: "If you've got so-called professionals in charge, they ought to win more often than not."

Atwater's effort to reach out to blacks has also run into snags—no surprise, considering that he engineered the Willie Horton campaign. He recruited Thelma Duggan, a black political strategist who was a Reagan White House aide. Her appointment is supposed to help position the GOP as the party of economic opportunity. But the message is being drowned out by controversy. Atwater was mortified when former Ku Klux Klan leader David Duke was elected to the Louisiana legislature as a Republican. And in March, black student protests forced the RNC chief to resign his new post as a trustee of Howard University.



ATWATER: LESS BRASH

SWITCHEROOS. Atwater is taking the difficulties in stride. "If we needed a few things to let everybody know we're in the middle of a trench war, that suits me fine," he says. "We're trying to change historical patterns, so I expect there to be numerous setbacks."

Atwater has made a bit of progress. A campaign to persuade southern Democratic officeholders to switch parties has had some success. In the biggest catch, Representative Bill Grant of Florida became a Republican in February, giving the GOP a majority in the state's congressional delegation. And in the past few months more than 50 state and local officials in six states have joined the GOP. "That more than compensates for other setbacks," contends Atwater.

These days you can't help but notice a bit of defensiveness creeping into the normally brash Atwater's tone. Not long ago he was living out a dream, reveling in political success and jamming with such blues legends as B. B. King. Now that he's started taking his lumps, Atwater may be humming a few bars from B. B.'s classic *The Thrill is Gone*.

By Richard Fly

PITAL WRAPUP

IR SAFETY

Airlines are squabbling with Transportation Secretary Samuel K. Skinner over how to pay for new anti-terrorist measures ordered by the government. Devices needed to sniff out plastic explosives will cost \$100 million one, and other equipment and additional personnel could drive the price even higher. Skinner says carriers would raise fares to cover the cost of expensive new detection equipment. The airlines argue that terrorist attacks, such as the bomb that downed an Am Flight 103 in December, are aimed against the government and that Washington should use general reve-

nues to beef up security. As an alternative, the industry would accept funding the safety measures by tapping into the \$6 billion surplus of the Aviation Trust Fund.

SPACE

The White House is trying hard to boost Vice-President Dan Quayle's stature as head of the new Space Council. Although President Bush had already decided on Rear Admiral Richard H. Truly as head of NASA, the White House let Quayle sign off on the decision. Quayle flew to Houston on Mar. 31, chatted with Truly, then called White House Chief of Staff John H. Sununu to O. K. the nomination.

HEALTH

Secretary Louis N. Sullivan is finally staffing up the Health & Human Services Dept. Sheila P. Burke, chief of staff to Senate Minority Leader Bob Dole, is slated to head the Health Care Financing Administration, which runs medicare and medicaid. The appointment was held up for weeks as officials checked possible conflicts involving Burke's spouse, former White House aide David L. Chew. Chew is a vice-president of Aetna Life & Casualty, a big medicare contractor. Former Office of Personnel Management Director Constance Horner will also move to HHS as Under Secretary.

This proposal to fund toxic waste cleanup is designed to keep the environment green.

One of the most crucial public policy problems facing America today is the gridlock that has tied up our national attempt to deal with toxic waste. Not only does this issue affect the quality of the environment, it represents a major economic challenge as well.

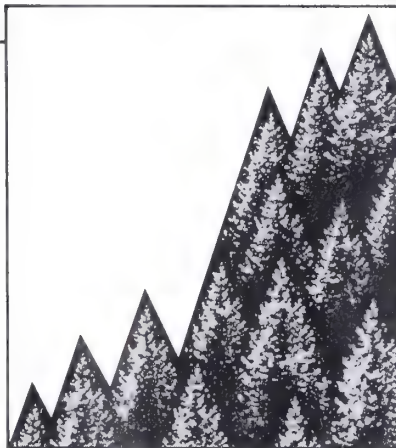
Studies by government agencies estimate that at least \$150 billion will be required to rectify hazardous waste sites that dot the U.S. landscape. Other research says that the costs could be higher.

This leads to the key question: How do we raise that amount of money without shackling the economy's ability to create jobs and compete internationally? As this suggests, economic forces are at the heart of the inaction on cleaning up the environment.

When the legislation designed to do that job—commonly known as Superfund—was renewed in 1986, the intent was to deal with the country's highest priority waste sites. Yet to date only a few of them have been addressed.

How did we reach this state and what can be done to change it? We must deal with four basic factors to answer that:

One: The current method used to assess and collect funds to clean up our old, known and often abandoned waste sites is founded on the principle of strict retroactive liability. This means that companies are being held responsible for environmental damage that occurred twenty or thirty years



ago, or even longer. That's true even when those companies did not violate any waste disposal laws, or act deliberately or irresponsibly.

Two: It is enormously costly and difficult—and sometimes impossible—to find out who is responsible for pollution at most older waste sites. The contamination occurred over decades and often the sites were common dumping grounds. Consequently, governments at all levels

are spending huge sums in their attempts to find polluters and fix liability.

Three: The staggering costs of cleanup are a major impediment to progress on improving the environment. The average price per waste site is \$25 million and can range up to several billion dollars. With stakes this high, it's impractical for any one party to bear the entire financial brunt of what amounts to a broad public problem. Even major corporations would be strained. The result? Fewer new jobs created and a reduced ability of American business to compete internationally. To be sure, we cannot look to government for more money given the federal deficit and the pressure on state and local government budgets.

Four: With the above three factors at work, our environmental efforts have bogged down in a morass of litigation. Most of the action is taking place in court, instead of at the waste sites. In some cases, even when insurers did not

And do the same for the economy.

cover pollution damage, there's been an inclination to look to the insurance industry as a public treasury when no other sources are available to pay the cleanup costs. But that's no solution since the total environmental price tag exceeds the surplus of the entire United States insurance industry.

A Proposed Solution

So we come back to the central question: How can we fund our national program to restore the environment? At AIG, we believe the answer lies in spreading the costs more broadly and equitably.

This could be accomplished if we created a National Environmental Trust Fund, which would be administered by the Environmental Protection Agency. This would be a dedicated fund whose resources would be used only to clean up hazardous waste sites.

The Fund could be financed by adding a separate, earmarked fee to the commercial/industrial insurance premiums now paid in the United States.

Even a modest assessment could provide enough money to deal with the 1,000 highest priority waste sites over the next decade. This approach would not require a new government agency



or new taxes. The fee would replace the current method of environmental taxation to give Superfund a new, more effective way to finance its mission.

The new Trust Fund would address only the old waste sites where responsibility for the pollution is not clear. Any environmental damage occurring in the future, or that resulting from deliberate acts, would be dealt with on a fault basis with the polluters paying.

The National Environmental Trust Fund thus recognizes the effects of past pollution as a national problem. It would avoid imposing an excessive financial penalty on any sector of business—or the economy as a whole. Most important, it would eliminate much of the endless litigation over pollution and enable us to get on with the job of cleaning up the environment.

This is a general outline of a new approach to an old problem. We've purposely presented it this way to stimulate a dialogue and to elicit ideas on the details of how a National Environmental Trust Fund should be implemented.

Please address your comments to: M. R. Greenberg, President and Chief Executive Officer, American International Group, Inc., 70 Pine Street, New York, New York 10270.

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AIG

THE NORTH AMERICAN SHAKEOUT ARRIVES AHEAD OF SCHEDULE

Cross-border consolidations are coming faster than anyone predicted

Within weeks of the U.S.-Canadian Free Trade Agreement going into effect on Jan. 1, the Inglis Ltd. unit of Whirlpool Corp. announced that it would stop making washing machines at its 108-year-old Toronto factory, eliminating 760 jobs. Instead, Inglis expects to import washers with newer technology from Whirlpool's sprawling plant in Clyde, Ohio.

And later this year, Whirlpool will shift a small part of its dryer production from Ohio to a newer Inglis plant in Ontario.

The Free Trade Agreement was widely expected to trigger such cross-border shakeouts. But as a unified North American market unfolds, a wave of consolidations is occurring faster and earlier than anyone predicted. Canada's tariffs against U.S. washing machines, for example, are scheduled to be phased out over 10 years, but Whirlpool decided to act now. In industry after industry, Canadian companies are merging among themselves or with U.S. companies to form giants (table). The push could accelerate as hundreds of companies flood U.S. and Canadian trade officials with requests to speed up the phaseout of tariffs on their products.

NO SMALL BEER. The consolidations are coming just as Prime Minister Brian Mulroney moves to pare Canada's federal budget deficit and possibly scale back some of Canada's vaunted social programs, such as unemployment insurance. Although the business restructuring will create more efficient North American competitors, one side effect is a less gentle Canadian economy. "The climate is not generous, not kind, for Canadian workers," says a spokesman for the Canadian Labor Congress. "It will be getting worse after the budget comes out."

Although Canadian critics have no immediate chance of overturning the free trade agreement, "it's going to remain a front-burner political issue," says Steven



WHIRLPOOL WILL STOP MAKING WASHERS AT ITS INGLIS PLANT

Blank, director of the U.S.-Canada business studies program at Pace University in New York.

Canada has traditionally had smaller companies in relatively fragmented industries. Canadians disdained what they saw as the more competitive, heartless style of U.S. giants. But even though beer was exempted from the agreement, the second- and third-largest brewers in Canada are hoping to merge. Spokesman Hershell Ezrin at No. 2 brewer Molson Cos. says it is only a matter of time before U.S. competitors get free access to Canada. Molson concluded that by merging its brewing operations with those of No. 3 Carling O'Keefe Ltd., it can prepare for a full-scale counterassault on the U.S. market.

Canadian Airlines International is playing the same strategy with its proposed purchase of a pesky discount competitor, Wardair International Inc. One of its motives was to end a price war in Canada, but the carrier also needs to bolster its balance sheet for what is likely to be the eventual battle for survival when U.S. and Canadian airlines are given unlimited access to each other's airports.

Organized labor is the biggest loser in these restructurings. Approval of an airline consolidation would lead to the elimination of 1,000 Wardair jobs and 600 at Canadian Airlines. Seven of the breweries will be closed and 1,400 jobs cut if the Molson-Carling consolidation gets the green light from Ottawa. Dominion Textile Inc. in Montreal announced it will eliminate about 1,000 jobs in Quebec because of reduced protection for its fabric operations. The union's move to merge its Caldwell towel division with C.S. Brooks Co.

BUILDING BUSINESS MUSCLE IN CANADA

AIRLINES Canadian Airlines International, No. 2 in market share, is buying No. 3 Wardair

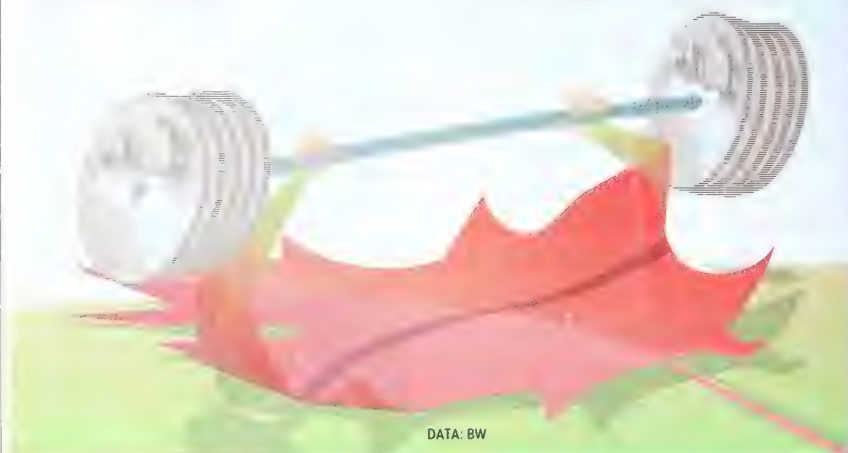
BEER No. 2 Molson proposes combining with No. 3 Carling O'Keefe Breweries of Canada

METALS Alumax announces plans for a \$1 billion aluminum smelter in Quebec

OIL No. 1 Imperial Oil, controlled by Exxon, purchases Texaco Canada

PULP AND PAPER Chicago-based packaging giant Stone Container will buy Consolidated-Bathurst of Montreal

STEEL Dofasco acquires Algoma Steel from Canadian Pacific, creating the largest steel-maker in Canada



DATA: BW

ew York will not create any new

ie imponderable is what sort of
U.S. exporters will score in Cana-
markets. A politically delicate field
decommunications, where tariffs
mostly disappeared. U.S. compa-
ranging from Telenet Communica-
a unit of U.S. Sprint Communica-
to American Telephone &
graph, want to crack the market.
Rooney, Telenet's vice-president
international operations, says he ex-
to announce soon a multimillion-
r, multiyear sale of telephone
hes. This market has long been
nated by Northern Telecom Ltd.

ILING NORTH. From Buffalo to Min-
polis to Seattle, hundreds of small
midsize American companies also
locking to seminars to learn how to
t to Canada. Dale K. Kicker, presi-
of tiny, \$1 million-a-year Bending
ches Inc. in Minneapolis, is finding
w going in his effort to sell canoe
ies and hockey sticks in Canada. In
it is because the Canadians "are
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s that better access to hockey play-
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uble his sales of hockey sticks. Oth-
omising sectors for U.S. exporters
urniture, textiles and clothing, elec-
machinery, and fabricated metals.
dian exporters also are gearing up.
porters of free trade worry that it
get blamed for cutbacks in Canada's
l programs. When Parliament re-
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that cutting the federal deficit
d be the top item on Mulroney's
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are higher than those in the U.S.,
pushing up the cost of servicing
ebt.

limit the damage, Mulroney is ex-
d to implement an austerity budget
month that will cut unemployment
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Axworthy, a trade critic in Parlia-
for the Liberal Party, says the re-
will be a government that is less
ng and compassionate."
ring or not, the reshuffling of the
h American economy will continue.
U.S. and Canada already are the
l's largest trading partners, doing
ast \$150 billion worth of business a
with each other. More than 4,000
s cross the Peace Bridge at Buffalo
day, and that two-way traffic is
to grow. As it does, the sorting out
ho is competitive—and who isn't—
only intensify.

Chuck Hawkins in Toronto and Wil-
J. Holstein in New York, with Mary J.
r in Minneapolis

POLAND

POLAND'S REFORMS MAKE GLASNOST LOOK LIKE WINDOW DRESSING

Warsaw calls elections and unshackles its economy



BARGAINING WITH WALESIA: THE COMMUNISTS HOPE TO PREVENT ECONOMIC COLLAPSE

Abruptly, after 43 restless years under Communist rule, Poland on Apr. 5 switched to a system much more like the market economies and pluralist democracies of the West. Under a pact signed by Warsaw's Communist leaders and the rebellious labor union, Solidarity, Poles will vote on June 4 in an election freely contested by legal opposition parties. They will choose a new Senate, or upper house of Parliament, and 35% of the existing lower house. Solidarity, legalized again, will reorganize as a nationwide movement. And Poland will once again have a President, chosen by Parliament, to dilute, if not replace, the authority of the Communist Party's chief.

This surprising political revolution began as "round table talks" on Feb. 6 aimed at easing a years-long deadlock between workers and the Marxist government. The immediate purpose was to save Poland's inflation-ridden and debt-burdened economy from collapse. General Wojciech Jaruzelski and other Communist leaders calculated that only a truce with a strong Solidarity, led by Lech Wałęsa, could head off disaster. But as the talks continued, "we realized that a historic compromise was necessary to stabilize the situation," says Communist Politburo member Jozsef Czyrek. "Union pluralism isn't enough. We also need political pluralism."

As part of the price of compromise,

however, Solidarity demanded and got an agreement to give workers wage boosts equal to 80% of the inflation rate, currently running at an 80% annual pace. Such "indexation" will fuel continued inflation, economists warn.

Still, the political freedoms are buttressed by a newly unshackled economy, liberated from state planning and monopolies by a sweeping Dec. 22 Law on Economic Activity. There is now no limit, for example, on the number of workers private companies may employ. "For the first time since the war, we recognized the equality of the state and private sector," says Andrzej Wójcik, secretary of state in the Foreign Economic Relations Ministry.

DYNAMISM. A powerful motive behind Poland's sharp turn is the need for help from Western creditors in easing the country's \$40 billion debt burden. Poland is asking U.S. support for a standby credit from the International Monetary Fund. And Bonn officials suggest that a big West German loan could highlight a planned visit by German Chancellor Helmut Kohl to Warsaw this year.

Despite economic liberalization, most big industry is likely to remain state-owned for years for lack of domestic capital to privatize it. But 80% of Poland's farms are still private, and many Poles hope that an upsurge in industrial entrepreneurship will give their economy some of the dynamism of Italy's, where

thousands of small companies flourish alongside state-run behemoths.

A second far-reaching law throws Poland's economy wide open to investors from abroad by allowing 100% foreign ownership of businesses. Under earlier legislation permitting joint ventures, Marriott Corp. is building a hotel in downtown Warsaw with local partners, and a venture by Hollywood's Hanna-Barbera Productions Inc. is turning out animated cartoons. Under the new law, Toolmex Corp. of Natick, Mass., last month took a 20% share in Tolfamex, a toolmaker in southwestern Poland. The aim is to double the production capacity of Tolfamex, which has been supplying cutting tools to Toolmex for 16 years. One issue that wasn't even discussed at

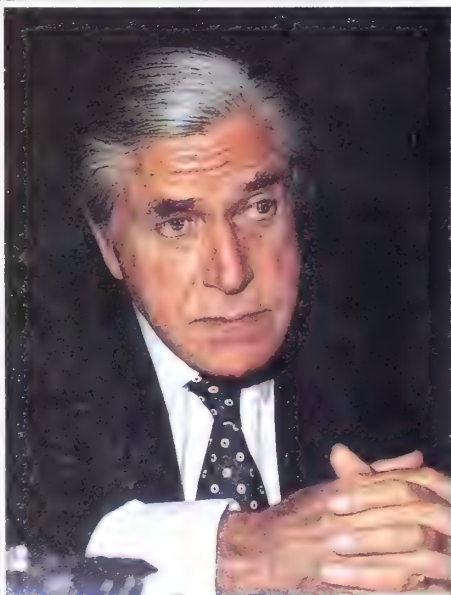
the round table, though, was Poland's membership in the Warsaw Pact, the Moscow-led military alliance. Provided that Poland stays loyal to that alliance, Soviet leader Mikhail S. Gorbachev has been encouraging Warsaw's Communists to make a deal with Solidarity. "Moscow's message to our government was: 'Don't be so careful. Do whatever is necessary to get your house in order,'" says Andrzej Stelmachowski, a leading lay Catholic who mediated the talks. Poland's solution, in the "European house" that Gorbachev envisions as the dwelling of the Continent's inhabitants, is to open more doors to the West.

By Bill Echikson and Sylwester Kruppa in Warsaw, Bill Javetski in Washington, and John Pearson in New York

BRITAIN

BANNED IN BRITAIN: A NEW CHAPTER IN THE HARRODS SAGA

The government outlaws publication of a secret report



ROWLAND AND MOHAMED AL-FAYED: THE EGYPTIAN COULD BE FORCED TO DIVEST HARRODS

The last time Britain's oldest Sunday newspaper, *The Observer*, printed a weekday edition was during the Napoleonic Wars. But on Thursday, Mar. 30, a 16-page *Observer* special edition was splashed across newsstands all over Britain.

No, it wasn't war or even peace but something dearer to the heart of the *Observer's* proprietor, tycoon Roland W. "Tiny" Rowland. Somehow, Rowland had obtained a copy of a secret government report that criticized his arch-enemy, Mohamed Al-Fayed. And his

newspaper rushed out excerpts. Furious government ministers quickly obtained a court order banning publication, but not before about 150,000 copies were sold.

Rowland and Al-Fayed have been conducting a public feud since 1985, when the Egyptian financier and his brothers snatched away a glittering prize that the tycoon had long coveted: Harrods Ltd., London's premier department store. The Al-Fayeds produced a \$1 billion cash offer for Harrods' parent, House of Fraser PLC, and quickly won government approval. Ever since, Rowland has claimed

the Egyptian was really a front man for the Sultan of Brunei and had lied to the government.

If Rowland's move was meant to create a stir, it succeeded. Lord Young, Britain's Trade & Industry Secretary, termed the publishing of the excerpts "unlawful and irresponsible." Claiming that publication would harm a criminal investigation, Young refuses to publish the report or allow others to do so.

HUMBLE ROOTS. According to the *Observer*, the excerpts are from an earlier government investigation into the Al-Fayeds. The findings as reported in a special edition are damning. Almost every claim by the Egyptians is demolished. For example, the Al-Fayeds told the government that they came from an old, wealthy family. But the inspectors say they're sons of a humble teacher.

At the time of the takeover, the Al-Fayeds and their advisers claimed that the brothers had more than \$1 billion in personal assets, which gave credibility to their all-cash bid. They much later revised that to \$760 million. But the inspectors call even the latter figure "exaggerated and misleading." Nor are they satisfied about the origins of \$400 million in cash that appeared in an Al-Fayed bank account in 1984. The Al-Fayed in 1987 claimed this was money from a breakup of a secret oil-trading partnership. But the inspectors debunk that assertion and say it was "untrue."

The report's conclusion: The Al-Fayeds probably received their money through their links with the Sultan of Brunei and weren't nearly as wealthy as they claimed. The Al-Fayeds "dishonestly misrepresented their origins, their wealth, their business interests, and their resources," the inspectors intone.

What the latest revelations mean for the Al-Fayeds isn't clear. Some critics argue that the source of the brothers' funds isn't important. But the government may not take so sanguine a view. Lying on takeover documents constitutes securities fraud. And lying to government inspectors is an offense akin to perjury. Even Lord Young admitted in the report "clearly disclosed wrongdoing." In theory, the Al-Fayeds could be forced to divest Fraser or to resign as directors, but the case could drag on for years. Al-Fayed did not respond to requests for comment.

As for Tiny Rowland, his lust was not for Harrods. "We want to see justice meted out and to establish that our claims we've been making for four years are correct," says Terry Robinson, a director of Rowland's company, Lorb PLC. If you're on a crusade like that, it helps to own a newspaper.

By Mark Maremont in London



Mahout trainer-wheels

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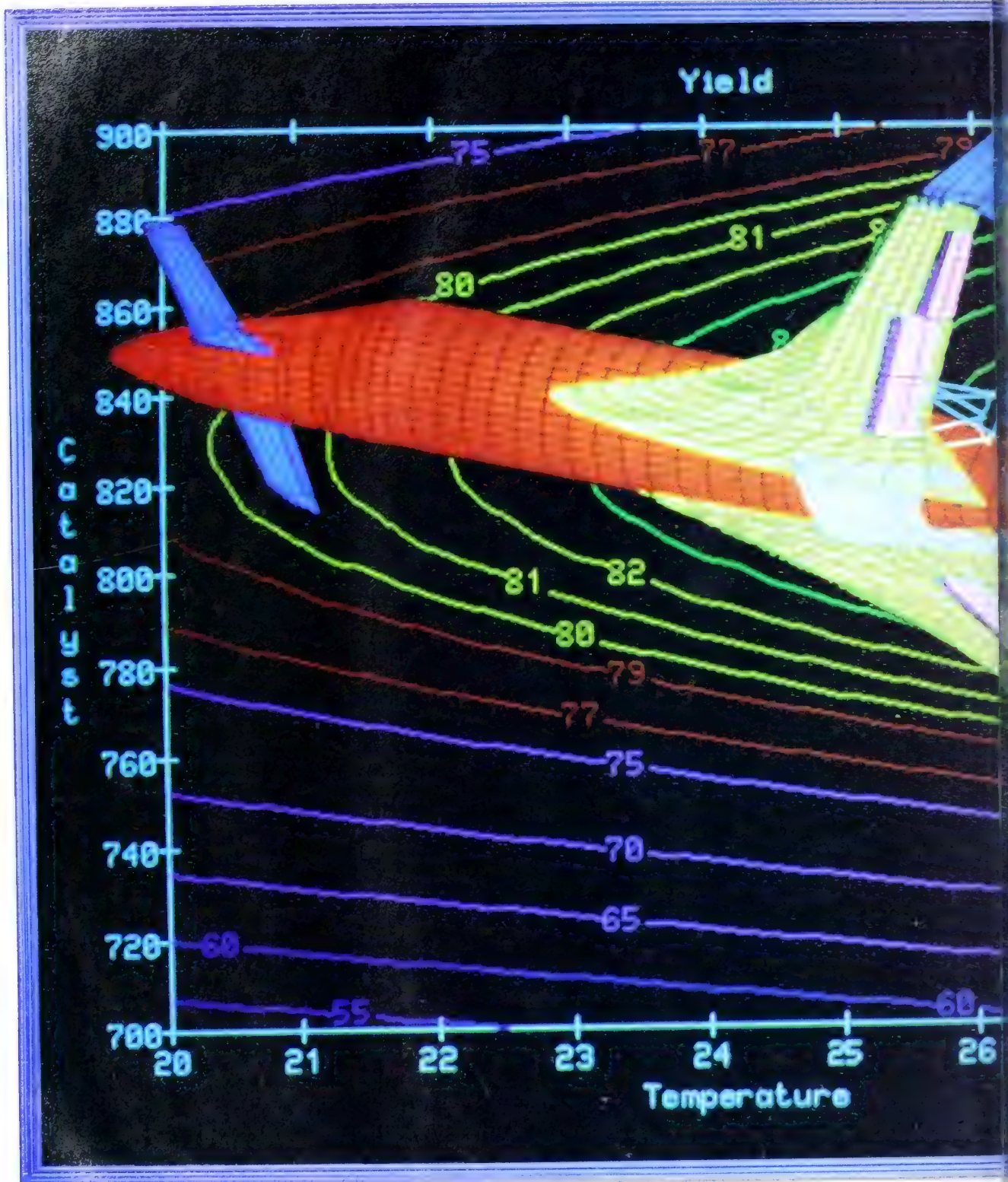


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WASHINGTON ISN'T MELLOWING ON CUBA—BUT MIAMI IS

Just before Mikhail S. Gorbachev's visit to Havana in early April, Secretary of State James A. Baker III informed U.S. embassies around the world that the U.S. has no plans to improve ties with Cuba. The memorandum, leaked to the press, seemed designed to head off speculation that the U.S.-Soviet détente might also warm up U.S.-Cuban relations. Despite Fidel Castro's agreement to pull troops out of Angola under a U.S.-mediated accord, Baker insists that relations won't get better until Cuba ends its support for Nicaragua. For decades the hard line on Cuba has found favor with Cuban exiles in the U.S. But that may be changing among a younger generation. A key target of Baker's memo is Miami's anti-Castro Cuban Establishment, which plays an important role in domestic politics. Miami Cubans are contributors to both Republican and Democratic campaigns, and the Cuban-American National Foundation, dominated by Miami Cubans, is a powerful Washington lobby. Following its success in getting the Reagan Administration to shut down Radio Martí in 1985, a current administration goal is to persuade Congress to shut down TV Martí to beam programs to Cuba in order to counter Castro's information monopoly. In Miami, at the same time, the anti-Castro exiles' influence has largely monopolized Spanish-language radio programs, keeping less rigid views on U.S.-Cuban relations off the air.

WARD BOUND. One sign of changing attitudes among the exiles is the shift in tone by some radio commentators who now simply refer to Castro by name instead of calling him "el malo" or "el déspota." More important, recent polls have shown that sizable majorities of Cuban-Americans favor negotiations with Cuba on issues such as human rights and family reunification. "Exiles will never like Fidel Castro," says John Skins University's Wayne Smith, who formerly headed the U.S. diplomatic "interests section" that operates in the Swiss

embassy in Havana. "But after 30 years there's a sense that it's better to reengage Cuba in order to resolve certain issues." These range from travel between the two countries—an important issue for the many exiles with relatives in Cuba—to mail service and payment for U.S. property seized by Castro. Looking ahead, some Miami Cubans are exploring business prospects, at the invitation of government officials in Havana, although no business will be possible until the U.S. lifts its economic embargo.

The changing attitudes are reflected in the customer base of

Francisco Aruca, president of Marazul Charters Inc., who flies some 250 people to Havana every week from Miami. The number is restricted by the Cuban government, but Aruca says he has 25,000 Cuban-Americans on his waiting list to visit Cuba, and the list is growing by 400 to 500 per week. He figures that the visitors spend an average of \$5,000 apiece during a week in Cuba.

That helps explain why Deputy Foreign Minister Ricardo Alarcón says Cuba regards the Miami Cubans as an "important asset." Beyond the current limited economic ties, what Alarcón is probably referring to is the small but growing movement, especially among younger Miami Cubans, to promote closer ties with Cuba despite exile leaders' hard-line rhetoric. But many Miami Cubans say the Havana government must first take steps to ease its repression. The Pro-Family Committee, set up last year, intends to lobby for expanded U.S.-Cuban contacts. The Institute for Cuban Studies, a maverick organization set up by María Cristina Herrera, a Miami academic, expounds the growing view that such contacts will do more than a U.S. diplomatic freeze to spur changes in Cuba. While Castro adamantly rejects Gorbachev's *glasnost*, he may be less impervious to influences from across the Florida Straits.

By Antonio N. Fins in Miami



A DOMINO GAME IN MIAMI'S LITTLE HAVANA

GLOBAL WRAPUP

SOVIET UNION

Mikhail S. Gorbachev's push for political pluralism may be raising new obstacles to multibillion-dollar ventures that U.S. companies propose to build in joint ventures with Soviet industrial ministries. Steps toward democracy and decentralization are giving more say on such projects to local groups, which may oppose them.

On Apr. 3, *Izvestia* published a letter criticizing Siberian petrochemical ventures such as those planned by Comstock Engineering, McDermott, and Mitsui. The letter, written by Soviet academics, warned that such projects are big polluters and threaten local so-

cial structures. In Siberia's Yamal peninsula, development of gas fields already has been stalled by local fears of damage to the arctic tundra.

Not long ago such opposition to Moscow planners was unthinkable. But last month's congressional election gave Soviet citizens a chance to speak up. In local elections scheduled for next fall, their voices may be even louder.

THIRD WORLD

Mexico and Venezuela have opened talks with bank creditors, hoping to be the first beneficiaries of Treasury Secretary Nicholas F. Brady's plan to ease Third World debt. Mexico's goal is to win debt-service cuts and new loans

totaling \$7 billion per year. But a key element of Brady's scheme is in trouble. European finance ministers, echoing Federal Reserve Board Chairman Alan Greenspan, are against using International Monetary Fund or World Bank money to guarantee debtors' interest payments to banks that accept write-downs or lower interest rates on existing debt.

However, such guarantees are the quickest way to reduce Latin America's \$25 billion annual capital outflow. Without them, banks are unlikely to accept the 30% debt reduction that Mexico needs by June, Treasury says, when it is likely to run out of foreign exchange reserves.

LACROSSE

WHAT'S AS GORY AS HOCKEY AND AS UPSCALE AS SQUASH?

The Major Indoor Lacrosse League is packing the yuppies in

John Driscoll, 32, leads a double life. Weekdays he trades securities for First Boston Corp. in Manhattan. But on weekends he trades his three-piece suit and briefcase for his shoulder pads and lacrosse stick. He then earns \$200 a game playing in the Major Indoor Lacrosse League. "It's a juggling act, and some of my colleagues think I'm crazy, but I love the game," he says.

Lacrosse, in which players use sticks with basketlike nets at one end to carry a hard rubber ball and hurl it into a goal slightly smaller than a hockey goal, is the oldest "organized" sport in America. The Six Nations of the Iroquois, who regarded the game as training for their frequent military forays against neighboring Indian tribes, were playing lacrosse before Columbus arrived. Sometimes whole tribes took part. Strategy called for each player to disable as many opponents as possible, and spilling of blood was actively encouraged. Lacrosse has become only slightly less violent in the centuries since then.

WEEKENDS ONLY Normally, modern lacrosse is played on a soccer-size field with 10 players to a side. What Driscoll and his colleagues play is indoor, or box, lacrosse with six-man teams. The three-year-old league lives by keeping player salaries low. Paychecks range from \$100 to \$200 per game, based on experience. So Driscoll is not the only one who must balance playing professional lacrosse with a full-time business career. Games are scheduled for weekends only, so players don't miss work. But if box lacrosse seems bizarre by the standards of just about any professional sport, it has plenty going for it, too. Many of its players—and avid fans—were students at such high-grade colleges as Johns Hopkins, Dartmouth, and Cornell—all of which have interscholastic lacrosse teams. Sponsors looking for an upscale sport uncluttered by competing ads can find it in indoor lacrosse.

The league is encouraged by its new sponsors. USAir and Thrifty Rent-A-Car System Inc. came on board this past season, just ended. Coors Light beer became the league's first sponsor last year and continues to be its largest. It's a good match for Adolph Coors Co. because the brewer's target audience—young, active, upscale males—frequents indoor lacrosse games.



ROUGH STUFF: IT STARTED AS A WAR GAME FOR THE IROQUOIS

The games are a curious mix of socializing and mayhem. Announcers often invite fans to a postgame party, usually held in a banquet room at a nearby hotel, to meet the players in person and have a drink. Meanwhile, on the artificial-turf courts, such ice hockey no-nos as slashing with the stick and cross-checking—holding the stick with two hands and ramming an opponent—are not only legal, but actively encouraged.

The game takes its toll on the stick-

men. John Tucker, a 27-year-old salesman for American Telephone & Telegraph Co. weekdays and a gladiator to the Philadelphia Wings on weekends, has this unenviable record for his two seasons in the league: two concussions, three broken ribs, a broken finger, and major knee surgery. The league provides medical insurance.

FREE TICKETS. You might think employers would be leery of employees who spend a relaxing weekend in a sticky arena around getting hit by a stick. But many believe that a person who is competitive in sports will also be competitive in the business world. "The only grief I get is work about playing lacrosse is about the record," says Rufus Clark, a 24-year-old bank loan officer who plays for the Baltimore New England Blazers. Some players even find ways to use their hobby in their careers: Gary Martin, a market

representative for Unisys Corp. in Philadelphia, sends his clients free tickets for Wings home games at the Spectrum.

The Major Indoor Lacrosse League broke even this season and hopes for a profit next year. Since starting out with teams in Baltimore, New York, Philadelphia, and Washington, the league has added franchises in Worcester, Mass., and Detroit. Ticket prices range from \$9 to \$15 instead of paying rent for their arenas, the teams get 60% of the gate and the sports facility keeps the rest.

The league can point to many signs of growth. Average attendance for the 1989 season, which ran from January through March, was 9,614 per game, up from 7,721 per game last year. And the past season the league televised 12 games over local cable systems out of a total 48 played. That's up from 10 last year and only five the year before. The fast action and brutal hitting make the sport a natural for television.

While bones are occasionally broken, that's not the only reason players hang up their sneakers. Perhaps the main one is marriage. Driscoll, who plays for the New York Salt, is one of the few married players, but says this season is probably his last. "Lacrosse has always been a big part of my life, but now my family and home are becoming my priorities," he says. Old lacrosse players don't die—they even fade away, as it turns out. He got married and made little lacrosse players.

By Robert Duffy in Boston

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TIME-WARNER IS WIRED FOR CABLE WARS

The combine could make a big push into basic programming

Time Inc. and Warner Communications Inc. already qualify as major powers in cable television. Their clout will grow if they merge into Time Warner Inc. But even that won't satisfy the two companies. They're bent on moving into the one area of the industry where they don't play a major role: basic cable programming. Time and Warner want to run some advertiser-supported channels that cable subscribers can watch for free—a service similar to MTV, ESPN, and USA Network.

Both companies have big plans for basic cable. Time's Home Box Office Inc. will launch an all-comedy channel this year. HBO is trying to take control of the operations at Movie-time, a service that airs lots of Hollywood news, interviews with film stars, and trailers of coming attractions. Meanwhile, Warner is working on a deal with Robert Pittman, the founder of MTV Networks Inc., that will probably take advantage of his cable expertise.

ROOM TO GROW. The move into basic cable would be an important expansion for Time and Warner. They are already among the top cable operators—the companies that hook up the hardware. Time has 3.9 million subscribers, making it the second-biggest franchise owner after Tele-Communications Inc. Warner ranks fifth, with 1.5 million subscribers. In addition, Time's HBO and Cinemax dominate one part of the programming business: pay cable, where viewers pay extra to see recent movies and specials.

Basic cable is the missing piece, and it looks attractive because the companies need new markets with more promising opportunities to grow. Warner can't count on the Big Three networks to pay much more for the TV programs that its studio produces. The networks are trying to cut costs, and may soon win the right to produce more of their own prime-time shows. And HBO is struggling

to expand its business. The number of cable families that paid extra fees for movie channels rose only 2% in 1988.

In comparison, basic cable looks like a happy hunting ground. Advertisers will spend about \$1.3 billion on basic channels this year, a 21% increase over 1988, says senior analyst Larry Gerbrandt of Paul Kagan Associates Inc. Ad sales could leap to \$2.8 billion by 1995. Basic cable channels also profit from the rising fees that operators pay to carry the most popular services.



to launch all-comedy channels, MTV and Columbia Pictures Entertainment Inc. haven't yet decided whether to take HBO. There's only room for one comedy channel, and cable subscribers could prove to be a tough audience.

UPPER EDGE. Time and Warner enter the battle with the cable equivalent of a clear arsenal. For starters, nearly every cable system in the country carries HBO. Franchise owners might find Time's new comedy channel virtually irresistible—the company gives them a break on HBO. If that's not enough to beat the competition, Time's and Warner's own cable franchises—especially their key ones in New York City—could strike a fatal blow. It's extremely difficult for a channel to woo decision-makers in the world capital of advertising and finance when they can't watch it at home.

HBO's Fuchs says he's confident that he'll be the winner in any showdown over a comedy channel. "Whoever's out there is going to run into a big n

TIME AND WARNER: BACK TO BASIC CABLE

Service	Percent owned (Time and Warner)	Subscribers (millions)
TURNER BROADCASTING SYSTEM		
CABLE NEWS NETWORK	13%	47.5
SUPERSTATION WTBS		45.0
HEADLINE NEWS		32.0
TURNER NETWORK TELEVISION		23.0
BLACK ENTERTAINMENT TELEVISION		
	16	20.7
MOVIE TIME		
	40	11.5

DATA: BW

Time and Warner could easily dominate this side of the programming business. The two companies already own big stakes in some important basic cable programmers (table). Time also has an agreement that could allow it to run Cable News Network Inc. should Ted Turner leave his company. Time executives talk openly and frequently about the post-Turner era, although he seems eager to stay.

Time and Warner would like to control more than one basic cable channel. HBO's chief executive, Michael J. Fuchs, is already contemplating the advertising deals he could make with several services. He envisions incentive plans for cable that would be similar to the one Time employs for its magazines: Advertisers win discounts when they boost their spending on Time's publications and cut purchases at the competition.

The power Time-Warner would have alarms some potential competitors. Indeed, two major programmers that want

chine," he says. MTV's CEO, Tom Freston, acknowledges that HBO's clout gives him pause, but wouldn't be a deciding factor. HBO is the nemesis of his parent company, Viacom International Inc., which operates the No. 2 pay-cable channel Showtime. Columbia Pictures declined comment on its plans, but industry executives say it has discussed its proposals with several leading cable operators.

While HBO prepares to leave audience laughing, Fuchs says he wants to control Movietime. He has prepared a tale that he says shows how HBO could improve the channel's programming. It would play to an interested audience: Time and Warner own about 40% of Movietime.

The power of Time and Warner may be challenged on Apr. 12, when Senator Howard Metzenbaum (D-Ohio) chairs hearings on the proposed merger. But for now cable programmers are prepared for rough going as Time and Warner get down to basic.

By David Lieberman in New York

Subsidiaries of

The Saudi Arabian Oil Company

and

Texaco Inc.

have formed a joint venture partnership

Star Enterprise

to refine, distribute, and market petroleum products

*Morgan Guaranty assisted in the negotiations and
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AGNOS: "PEOPLE DIDN'T LIKE BEING TOLD WE WERE BROKE BY SOMEONE THEY THOUGHT WAS GOING TO MAKE THINGS BETTER"

ART AGNOS: SCAPEGOAT BY THE BAY?

Almost everybody has a gripe with San Francisco's mayor

As San Francisco Forty-Niners quarterback Joe Montana began his steely-eyed touchdown drive in the waning minutes of Super Bowl XXIII, one Niner fan had more than the point spread on his mind. "I was a wreck," admits San Francisco Mayor Art Agnos, who was sitting high above the field in a luxury box. "I thought, 'Oh no, we're gonna lose, and the entire city will be in a foul mood and blame me.'"

Hizzoner had good reason to feel touchy. Slightly more than a year ago, Agnos, 50, swept into power with 70% of the vote. His pro-neighborhood, anti-growth platform thrilled staunchly liberal San Francisco. As business interests harrumphed, activists cheered to see their agenda on the rise again. But Agnos quickly found himself in a budget mess he hadn't bargained for. He has also taken heat for a grape boycott that has driven away convention business and for taking stands that could exacerbate a corporate flight that has plagued the city since the early 1980s.

Agnos had barely decided where to hang family pictures in the oak-paneled

mayor's office when city accountants confronted him with predecessor Dianne Feinstein's bright red legacy: a budget deficit of \$180 million, at least double most preelection estimates. Suddenly there was no money to fund his promised programs for improved public health services, help for the homeless, job creation, and affordable housing.

'GREEN EYESHADES.' Agnos' liberal play-book was useless. Instead, he had to call for a quick budget slash to stave off insolvency. Libraries were closed. Police and fire departments took cuts. Business had to pony up an extra 0.1% payroll tax. And city workers' wages were frozen. "People didn't like being told we were broke by someone they thought was going to make things better," Agnos admits ruefully. A year later the mayor has won quiet praise from many quarters for slicing \$100 million off the deficit in 1988. He notes that his plan impressed the "green eyeshades from New York" enough to keep the city's Standard & Poor's bond rating at AA.

But fiscal conservatism has yet to win Agnos a place in the city's heart. While

moderate "Lady Di" Feinstein—now running for governor—basked in constant, almost adoring press coverage, Agnos spent most of his rookie years behind closed doors, slaving over the budget, trying to head off three separate strikes, and quieting volatile racial disputes in the fire department. In a city with a tradition of rah-rah mayors who love the limelight, that hasn't gone too well. Some critics call him "Art Anonymous." *San Francisco Chronicle* columnist Herb Caen uses the term "gnosis"—a disease afflicting those who voted for the mayor "but can't remember why."

It's not as if he's a newcomer. The son of Greek immigrants, Agnos arrived in San Francisco 23 years ago after finishing a master's degree in social research at Florida State University. He has worked in the city housing authority, then held several jobs in state government. In 1977, Agnos began an 11-year career as a state assemblyman.

In private meetings, Agnos is witty, and personable. Friends and fans praise his willingness to listen. But Agnos puts a lot of responsibility in his deputies' hands. And he prefers spending his free time with his wife and sons to hobnobbing with the elite at downtown functions.

It's hard to figure just what business leaders expect from the mayor. Business has the deficit to thank for its tax hike. And while Agnos has formed a small business council to address the city's notoriously molasses-paced permit process, he can't do an about-face on such issues.

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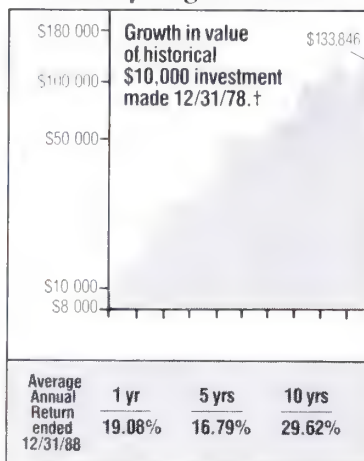
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†Total returns include change in share price, reinvestment of dividends and capital gains and the effect of the fund's 3% sales charge. The fund's share price and return will vary, and you may have a gain or loss when you sell your shares. Average annual total returns for more than 1 year assume a steady compounded rate of return, and are not the fund's year-by-year results, which varied over the periods shown.

Government

as rent control and slower down growth, which helped elect him.

Rather, it seems to be City Hall stands on such issues as gay rights, apartheid, and Northern Ireland that really set business' teeth on edge. Recently, the Chamber of Commerce attacked Agnos for a city boycott of Central California grapes on the grounds that pesticides used on the grapes hurt farmworkers. The Chamber says that cultural groups have canceled \$60 million worth of convention business. The San Francisco Hilton alone claims to have lost \$1 million in the backlash.

Agnos has even drawn darts from such staid corporate citizens as Chevron Corp. In a recent speech, Chairman Kenneth T. Derr complained: "The business community has been given the back of the city's hand." Chevron is still stirring from city supervisors' 1986 apartheid resolution banning San Francisco from doing business with Chevron because of its ties to South Africa. "Are these city issues?" Derr asks.

As business has fled, the city fears the impact of losing out to Los Angeles as a Pacific financial center.

Business leaders say they're trying to protect San Francisco's image. In the past decade, the city has lost a slew of major corporations: Crown Zellerbach, Pacific Lumber, Castle & Cooke, D.M. Monte, Fireman's Fund, and Southern Pacific. Most resulted from mergers or takeovers. But the flight has fueled perceptions that San Francisco has lost its luster, particularly to the rising financial center of Los Angeles. Tricia Jamer, director of the South of Market Business Assn., says City Hall's indifference has created "an erosion of spirit" that will drive still more companies away.

The mayor says the numbers are on his side: "We've been hearing this for 10 years, but I don't buy any of it. He maintains that San Francisco remains a vibrant source of growth, particularly because of its location on the Pacific Rim. United Airlines Inc. has plans to make the city its Pacific hub, adding 1,000 jobs and \$100 million to the economy. With unemployment at 3%, Agnos insists: "We're experiencing a boom in our economy, not a decline. While business leaders may disagree with him, it's in their interest to put him right.

By Joan O'C. Hamilton in San Francisco

The Columbia Gas System, Inc.

*through its wholly owned subsidiary,
Columbia Gas Development of Canada Ltd.,
has sold its offshore Canadian oil and gas assets to
Chevron Canada Resources,
a wholly owned subsidiary of*

Chevron Corporation

*Morgan Guaranty initiated this transaction,
assisted in the negotiations,
and acted as financial advisor to
The Columbia Gas System, Inc.*

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JIM KINNEAR IS PUMPING NEW LIFE INTO TEXACO

He has lifted the stock price and worker morale, but a raid may be just a matter of time



KINNEAR: A PROMISE TO PAY \$2 BILLION IN SPECIAL DIVIDENDS HAS CHEERED SHAREHOLDERS

Texaco Chief Executive James W. Kinnear is feeling bullish. He recently finished a series of whirlwind trips to dozens of Texaco operations from Central America to Southern California. Everywhere he was met by waves of eager Texaco employees. In Port Arthur, Tex., once a hotbed of labor unrest, union refinery workers have even named a street after him. "There's a lot of adrenaline running through Texaco," he says. "This is a new company."

Kinnear, 61, must feel like new himself. After a five-year battle to save Texaco Inc. from bankruptcy court and corporate raiders, he's finally able to get down to business. A pact to pay out \$2 billion in special dividends and buy back \$500 million worth of stock has cheered shareholders. Ditto for Texaco's earnings, which spurted ahead last year because of strong refining profits and the CEO's restructuring efforts. Kinnear has even managed to appease nemesis Carl C. Icahn. Although the takeover artist still owns 17.2% of Texaco's stock, he has signed a seven-year standstill agreement. Says PaineWebber Inc. analyst

Bryan Jacoboski: "Texaco's starting to turn around."

Maybe. But Kinnear's not out of the woods yet. Even after selling or writing off \$9 billion worth of assets, Texaco is still trading at only 60% of its breakup value, according to some analysts. Its U.S. energy reserves alone could fetch close to \$12 billion—about equal to Texaco's market value. Throw in a 50% share of Caltex, the Texaco-Chevron joint venture with vast oil and gas reserves, refining operations, and real estate holdings, and the tally is \$16 billion. Investors needn't look far for examples of Texaco's bustup potential. In December the company sold its Canadian division to Exxon Corp. for \$3.2 billion, or \$1 billion more than anyone had hoped.

Kinnear's moves have helped boost Texaco's share price from \$38 a year ago to \$53 recently. That price is

partially buttressed by the promise of \$1 per share in special dividends—the last of which will be paid in September. Moreover, though Icahn's agreement keeps him from bidding, some industry sources believe he backed down only because he knew of interested companies that might eventually buy him out. Icahn isn't talking. But a source close to him says: "If Kinnear doesn't [perform] someone will still come in and do it for him. It's just a matter of time."

'HORROR SHOW.' Shareholders have pressured Texaco into replacing its poison pill with a weakened version that allows for an all-cash bid, opening the door to a suitor with deep pockets. The proposal is expected to be adopted at the company's May 9 annual meeting. Among Texaco's competitors, Chevron Corp. has been mentioned as a possible bidder. Some analysts think an investor willing to spin off Texaco's varied assets could emerge as well.

Texaco has been takeover bait ever since it found itself on the wrong side of an \$11 billion judgment in its epic court battle with Pennzoil Co. But the root run deeper. When Saudi Arabia nationalized the company's oil production facilities in the early 1970s, cutting deeply into production profits, Texaco didn't move as quickly as its competitors did into such frontier areas as Alaska and the North Sea. Nor did it streamline its U.S. marketing operations; instead, it clung to its 1960s strategy of serving a 50 states. Left with poor reserves and thousands of unprofitable gas stations, Texaco limped into the 1980s. "It was a horror show," says Jacoboski.

Texaco hoped to end the nightmare by snatching Getty Oil Co. in 1983. But its price had already signed a merger agreement with Pennzoil. For \$8 billion, Getty nearly doubled Texaco's U.S. reserve base. But it also led Texaco into court, Chapter 11, an almost into Icahn's arms. In December

TEXACO'S ACHILLES' HEEL

Company	Reserves* Years
MOBIL	13.1
AMOCO	12.8
ATLANTIC RICHFIELD	12.0
EXXON	11.3
CHEVRON	11.1
TEXACO	8.7
INDUSTRY AVERAGE	12.0

*Worldwide oil and gas reserves based on 1988 production levels

DATA: ENERGY PERFORMANCE REVIEW



General Motors Corporation

and

Corporación Metalmen, C.A.

have formed a joint venture

Empresa Mixta General Motors, C.A.

to assemble and distribute General Motors products in Venezuela

Morgan Guaranty assisted in the negotiations

and acted as financial advisor to General Motors Corporation

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The Corporation

near was named CEO, a shareholder committee pushed him to finally settle with Pennzoil for judgment," he says.

The outcome forced a drastic overhaul of Texaco's operations and management. In addition to asset sales, Kinnear has slashed Texaco's worldwide payroll by 30%. He has turned Texaco's 26 U.S. divisions into 13 independent profit centers, cutting two layers of management between the field and the company's headquarters in White Plains, N.Y. He has also slated a new stock incentive plan for 500 Texaco executives tied to performance and has set up joint

to study plant problems. Employees love it. "He's the first CEO with the guts to come down here," says Jerry Sparks, a top local official of the Oil, Chemical & Atomic workers in Port Arthur.

CAR WASHES. Kinnear, an Army graduate who served in the Korean War, is a career Texaco man. He made his mark reviving the company's refining and marketing units, starting in 1982 when he became president of the huge Texaco USA division and finishing the job when he became CEO in January, 1987. He has since jettisoned seven money-losing refineries and 2,500 gas stations, while exiting 11 states. He cut costs by equipping Texaco's remaining seven

But the most novel part of Kinnear's restructuring was a deal inked with the Saudi government this year. He folded 60% of Texaco's U.S. refining and marketing operations into a joint venture with Saudi Aramco, receiving \$1.1 billion in cash, 22.5 million barrels of crude inventories, and a steady flow of oil for three of Texaco's refineries for the next 20 years. These moves "tie us to the largest oil supplier in the world," crows Kinnear.

That's an important linkup because Texaco has one of the worst drilling records among the giant oil companies—



PROFITS AT TEXACO'S DOWNSTREAM OPERATIONS ARE SOARING

its reserves far behind other majors (table, page 50). Texaco intends to improve its record by drilling more wells in existing fields rather than exploring in new areas. In the U.S. it will target 60% of its drilling on such properties vs. 40% last year. "In the past, we tried to do it all," says Elton G. Yates, head of world-

wide operations. "Now we're focusing our operations."

Already Texaco's field costs have fallen from the industry's highest to among the lowest, at \$3.33 a barrel. For the first time in many years, the company replaced all the oil that it produced in 1988, 87% of that came from new existing fields, not finding the frontier.

Such a strategy will boost short-term earnings, says Kinnear's watchful shareholders. But to keep up with rivals over the long haul, Texaco desperately needs some discoveries. Kinnear has a task force to identify a few frontier regions, such as the Chukchi Sea, north of Alaska, which some experts hold a rich 3 billion barrels

oil. Still, as consultant Kurt H. president of McDep Associates points out, "Texaco has to run twice as fast [as the industry] just to catch up." After Jim Kinnear's battles with a ruptured court and a raider, that must be a welcome challenge.

By Mark Ivey in White Plains

TRANSPORTATION

THE LOFTY DREAMS OF UPSTART AIR EUROPE

Harry Goodman's low-cost assault on Europe's big boys

Remember Sir Freddie Laker and his transatlantic burnout? Well, now another English entrepreneur and big-time dreamer, Harry Goodman, is storming the heavens. Goodman wants to build the dominant low-fare carrier in Western Europe. Whatever the ultimate fate of his Air Europe

Ltd. is clearly going to give its competitors a run for their money.

Already, Air Europe offers scheduled service to the Continent from Britain than any other airline save British Airways PLC. Goodman runs flights a week from Gatwick to a number of cities. He sets fares as much as 50% below those of established carriers.



AIR EUROPE ALREADY SERVES 13 CITIES

TF Investments, Inc.

has acquired through a leveraged buyout

Hospital Corporation of America

*Morgan Guaranty assisted in the negotiations
and acted as financial advisor to*

*TF Investments, Inc. J.P. Morgan & Co. is an
equity investor through Morgan Capital Corporation.*

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Goodman has orders and options worth \$3.5 billion for 75 planes from Boeing, Fokker, and McDonnell Douglas. By 1994, Goodman's fleet could have about 100 aircraft. That would rival Swissair, Europe's seventh-largest airline.

Air Europe is just the latest chapter in the Dickensian saga of the 49-year-old Goodman, the son of a sweatshop worker in London's East End. Orphaned at 13, Goodman started as a gofer in a travel agency at 16 and founded his own agency a decade later. He soon started to operate tours, pioneering cut-price packages for Britain's working-class tourists. Last year, Goodman's International Leisure Group PLC (ILG) sold 2.5 million vacations, about 20% of the British market.

TOUR SLUMP. Along the way, Goodman developed a reputation as a self-promoter with a taste for the good life. Seven years ago an arrest for cocaine possession, which resulted in a fine, ended the high living. Now, Goodman says he is a teetotaler and leads a quieter life with his third wife. He even sold his 170-foot yacht last year.

Goodman is ready to move from dependency on the tour trade. After years of healthy growth, the package-tour industry in Britain stagnated in 1988 and could shrink 10% in 1989. ILG's tour unit had only \$4.9 million in operating profits last year on \$840 million in sales.

Spotting a huge opportunity in the deregulation of Europe's skies, Goodman is focusing nearly all his energies on Air Europe. Unlike many new carriers, Air Europe is not starting from scratch. It has been operating as a charter airline since 1979 and last year carried 1.5 million charter passengers. The charter business provides

Holiday Inn franchise," says Goodman. "We have complete control over fleet, standards, philosophy, and operations." He figures that he can take majority control—and create a pan-European carrier—if the curbs on foreign ownership disappear.

Goodman has gained precious access to some of Europe's busiest airports by investing only \$10 million in small airlines in Spain, Norway, and West Germany. Startups with local partners in France and Italy will follow. In each country he intends to begin as a charter carrier, bring in a local tour operator as a partner to ensure sufficient bookings, and then ease into scheduled service. One market Goodman will avoid: the competitive transatlantic corridor, where Freddie Laker's airline foundered.

HARRY GOODMAN'S TRAVEL KINGDOM

Through a holding company Goodman controls International Leisure Group PLC. Operations include:

ILG TRAVEL LTD. Britain's second largest tour operator, with sales of \$840 million

AIR EUROPE LTD. British airline providing European service: Sales are \$390 million

PLAYCOSTA Small Spanish hotel chain

AIR EUROPA Spanish airline, 25% owned by ILG

NORWAY AIRLINES 33% owned by ILG

HUXENBERGER FLUGDIENST German commuter airline, 49% owned by ILG

DATA: COMPANY REPORTS

If Goodman's schemes work, his no-union work force and small office staff would give him a big cost advantage over Europe's big carriers, which have long been cosseted against competition. And Goodman believes that he gets more revenue from his planes than his big competitors, because he uses the same craft to fly scheduled service during the day and charter flights late at night. A spokesman for SAS figures that Goodman's costs could be as much as 20% lower than those of his large competitors. "The people terrified of Harry are the high-cost operators," says Richard Hannah, airline analyst at UBS Phillips & Drew Ltd. in London. "If and when true deregulation happens, he can undercut Lufthansa by an enormous degree."

But if Goodman grows too successful, the big flag carriers may well match Air Europe's fares, whatever the cost. Says Sir Adam Thomson, former chairman of British Caledonian Airways Ltd.: "I don't see Air France or Lufthansa letting anybody take their market away without a good fight."

STRATEGIC RETREAT. Goodman also will have to worry about keeping his finances sound. Because of earlier purchases and a decision to take ILG private in mid-1987, he is already shouldering more than \$350 million in long-term debt and other obligations. As a result Goodman is paying for his big new plan order with some fancy off-balance-sheet financing.

Dicey as this strategy may be, Goodman will probably land on his feet. In 1985 he got into the hotel business. Two years later he got out—at a \$60 million profit. If the airline business gets too tough, Goodman might just sell his planes and gates and move on. "The essence of Harry

the carrier with valuable experience plus profits to compensate for initial losses from scheduled service. In fiscal 1988, Air Europe posted operating profits of \$32 million on sales of \$390 million.

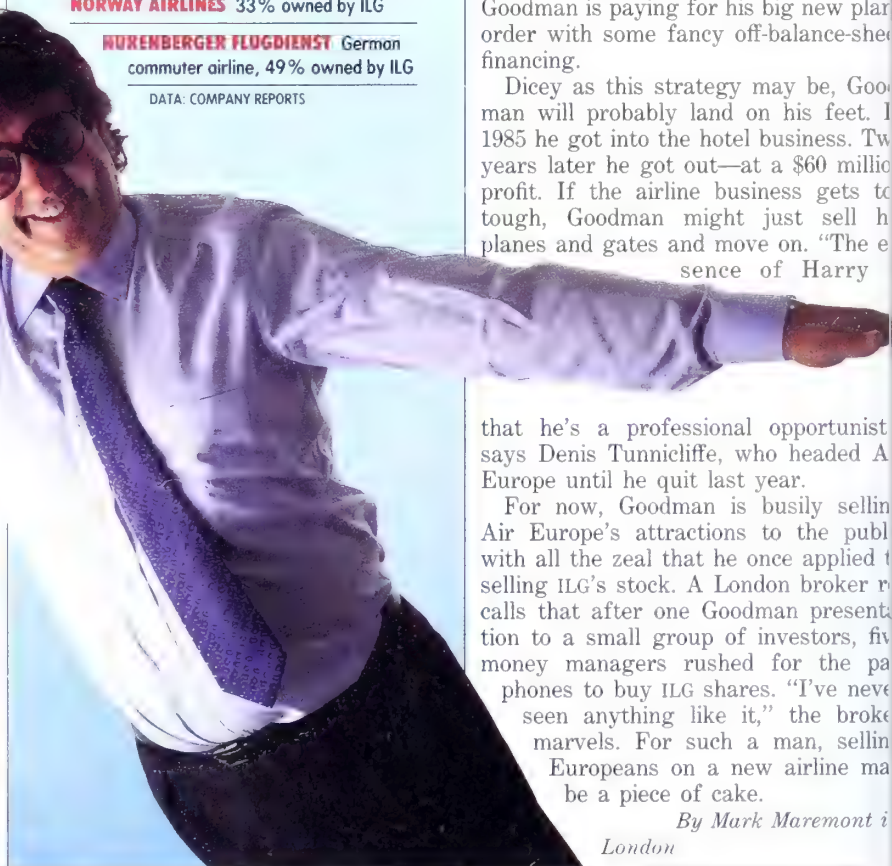
As Europe prepares to become a single market in 1992, the trick for Goodman is to set up hubs across the Continent. He has already figured out how to avoid the restrictions that countries such as France and West Germany now place on foreign control of airlines. He is creating a network of small carriers, each minority-owned by International Leisure Group, but all operating under the name Air Europe and flying some of the planes Goodman has ordered. "It's like a

that he's a professional opportunist," says Denis Tunnichiffe, who headed Air Europe until he quit last year.

For now, Goodman is busily selling Air Europe's attractions to the public with all the zeal that he once applied to selling ILG's stock. A London broker recalls that after one Goodman presentation to a small group of investors, five money managers rushed for the payphones to buy ILG shares. "I've never seen anything like it," the broker marvels. For such a man, selling Europeans on a new airline may be a piece of cake.

By Mark Maremont in

London





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SEMICONDUCTORS

NOW ENGINEERS DON'T HAVE TO ORDER OUT FOR CHIPS

With programmable logic devices, they can design their own

Ordinarily, it would have been hair-pulling time for Matthew Castrigno, a design engineer for Network Equipment Technologies Inc. He had put 10 weeks into building a prototype printed-circuit board that would enable networked computers to communicate over phone lines. Then, at the last minute, he uncovered a bug in a chip he had designed. Had the flaw been in a chip that was custom-made by an outside supplier, Castrigno would have had no choice but to fix the circuit design and twiddle his thumbs for a month or so until new silicon could be delivered.

Instead, he cooked up his own revision in just two hours. First, Castrigno corrected the chip's circuitry on the screen of his personal computer. Then he grabbed a so-called programmable logic device (PLD), a sort of silicon counterpart to Polaroid film, and plugged it into a special programming box. In less than two minutes the box plucked the new circuit design from his PC and transferred it onto the chip. This time the networking board worked fine.

PERSONALITY CELLS. To Castrigno's Redwood City (Calif.) company, that kind of instant turnaround has made PLD technology indispensable. "We couldn't exist without it," he asserts. And NET is hardly

alone. In fact, PLDs have become one of the hottest segments of the semiconductor industry (chart, page 58). The reason is simple: In the fast-paced world of computers and other chip-based gadgets, following the leaders to market by more than a few months can mean red ink for an entire generation of a product.

Equally important, when engineers know they can quickly change a chip's design, they are far more willing to gamble on creating innovative logic circuits. Programmable logic chips boost a

microprocessor's number-crunching power to provide a product with a distinct "personality"—features that can command a higher price for a given computer, video game, laser printer, or fax robot. Because the cheapest custom logic chips represent an up-front cost of \$50,000 or so, notes Robert L. Greup, product development manager at Instruments Inc., "an engineer is putting his career on the line" without design. But with a PLD, "he can erase his mistakes."

Kirk Owyang, an engineer with Inc., a Sunnyvale (Calif.) company, helps military contractors design receivers, notes that engineering typically have more than one opinion on the best chip design. With gate arrays and other "semicustom" logic chips, one design must be picked because producing multiple prototypes would cost too much time and money. "Before we just yell at each other until one of us won," says Owyang. But now, "we

started to take more risks." **WASTED SPACE.** Programmable logic devices have been around for a decade, but until a couple of years ago the most common of them had only hundreds of transistors—too few for a snappy "personality" to a product. The most common type, programmable array logic (PAL), was pioneered by Intel Corp. and Monolithic Memories Inc., since acquired by Advanced Micro Devices Inc. AMD, PALs continue to expand land-office business: \$339 million in sales last year. Although the company has been losing ground because it has been slow to update the PAL, AMD is still on top of the programmable logic heap, with more than triple the sales of No. 2 Texas Instruments.

But PALs have an info

DO-IT-YOURSELF COMPUTER CHIPS

Logic chips that can be programmed mean new flexibility for product designers. Here's a glossary:

PROGRAMMABLE ARRAY LOGIC (PAL). These chips are cousins of programmable read-only memory (PROM) chips, which hold the "wake-up" program that computers read when they are first turned on. Here the technique creates logic circuits, which help execute programs

ERASABLE/PROGRAMMABLE LOGIC DEVICE (EPLD). These are based on the technology used in erasable PROMs, which can be wiped clean with ultraviolet light. With EPLDs, engineers can quickly revise logic circuits on the chips

ELECTRICALLY ERASABLE/PROGRAMMABLE LOGIC DEVICE (EEPLD). As with their EEPROM cousins, circuits can be created or erased just by sending special signals that turn groups of transistors on or off

PROGRAMMABLE GATE ARRAY (PGA). The newest type, these chips adapt random-access memory (RAM) techniques. Some PGAs can be programmed just by loading them with logic-circuit design data from a floppy disk

DATA BW



Presto Industries, Inc.

has been acquired by

Reynolds Metals Company

*Morgan Guaranty assisted in the negotiations
and acted as financial advisor to
Presto Industries, Inc. in this transaction*

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density limitation. Every transistor is connected to its surrounding neighbors, and on each link is a tiny fuse that takes up extra space and prevents the circuitry from being packed as tightly as on conventional chips. An engineer carves out a logic circuit the way a sculptor chisels at a block of marble, blowing away fuses on the connections he doesn't want.

To provide more design freedom, a handful of innovative startups began pioneering ways to make PLDs that can be crammed with more so-called gates, decision points (a gate consists of multiple transistors). Castrigno of NET, for example, used an erasable PLD, or EPLD, for his data-communications board. Inspired by Altera Corp., EPLDs replace fuses with "programming elements" which are borrowed from erasable read-only memory (ROM) chips.

MORE ONE-OF-A-KIND CHIPS

SALES OF PROGRAMMABLE
LOGIC DEVICES



▲ MILLIONS OF DOLLARS
DATA: DATAQUEST INC

Next came EEPDs, or electrically erasable/programmable versions. Logic circuits are formed on these chips simply by sending special programming signals to each gate—an "on" signal incorporates that gate into the circuit, while "off" signals blocks it out.

But the technology that's really turning the market is the programmable gate array, or PGA. Basically, the chips are counterparts to the gate arrays that dominate the fast-growing market for customized chips called application-specific integrated circuits (ASICs). Regular gate arrays are featureless grids of thousands of gates, atop which the chipmaker lays down a customer's proprietary design. PGAs provide similar design versatility, with gate counts up to 9,000.

The PGA concept was pioneered by Linn Inc. The startup, based in San Jose, Calif., decided to go one-up on EPLDs by borrowing the technology used in random-access memory (RAM) chips. Transistors on these common memory chips can be packed more densely than ROM circuits. In addition, the design can be "mapped" onto the chip from software. That means equipment builders can easily



The Procter and Gamble Company

has acquired a controlling interest in

Perfumarias Phebo S.A.

*Morgan Guaranty acted as financial advisor to
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ly modify or upgrade systems already sold to customers by simply mailing a floppy disk containing the new circuit design.

For instance, Tektronix Inc. began marketing three new computer printers in January. All three are controlled by the same printed-circuit board. But a different program is fed to the PGA via the user first hooks the printer up to a computer. Tektronix can add more printers to the line and run them off the same board. And if it develops a circuit design to improve performance perhaps by offering more type fonts, upgrading the existing machines will be a snap, via the Post Office.

PGA TOURNAMENT. Because of the advances in PLDs, Dataquest has revised its sales projections—radically. The Jose market researcher now predicts that PGA sales will soar to \$507 million in 1994, from \$28 million last year. That's triple last year's estimate. Andrew Rappaport, president of Technology Research Group Inc., a Boston market researcher, believes PGAs will capture 10% of the gate array market. "That's the most exciting thing going on in the semiconductor field right now," he says.

But EPLD makers are battling to catch up with larger-capacity chips. A year ago Altera rolled out a chip that can pack as many as 5,000 gates. Last summer startup Actel Corp. in Sunnyvale topped that with 6,000 gates—although the number of gates is only one factor in a PLD's performance. Several more newcomers are now gearing up to enter the market.

New PLD products may help to infiltrate some older segments of the semiconductor business. Late last year Texas Instruments and Actel agreed to swap technologies. Dataquest speculates that TI will try to apply Actel's approach to its family of building-block circuits producing possibly a microprocessor with built-in do-it-yourself modules.

Today, programmable logic chips appeal particularly to smaller companies because they offer a new economy of scale. Conventional gate arrays can be much cheaper—just a few dollars each if bought in lots of 10,000. But in small quantities the price skyrockets because of that fixed \$50,000 front-end cost. Less than 1,000 chips, PLDs can be cheaper, even at prices of up to \$100 each.

Tomorrow may be a different matter. Some big companies, such as Unisys and Sun Microsystems Inc., are already on programmables. They believe getting to market sooner is worth the higher cost. Soon, most companies will figure they, too, can do it better with a do-it-yourself approach.



Ford Motor Company

through its wholly owned subsidiary;

Ford Indústria e Comércio Ltda.,

has sold its Brazilian consumer electronics companies,

Philco Radio e Televisão Ltda., Philco da Amazonia Ltda.,

and Philco Componentes Ltda. to

Investimentos Itaú S.A.—ITAUSA

Morgan Guaranty initiated this transaction

and acted as financial advisor to

Ford Motor Company in this transaction

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Developments to Watch

EDITED BY OTIS PORT

IS INTEL ABOUT TO CRUNCH CRAY'S NUMBER-CRUNCHERS?



By the mid-1990s the Defense Dept. wants computers that are 1,000 times more powerful than anything now available from Cray Research Inc. That's a tall order, given that the speed of Cray's processors has increased less than 10 times over the past decade. Even ganging together several processors in parallel has produced gains of less than a hundredfold.

But Intel Corp.'s Scientific Computers unit in Beaverton, Ore., figures it can deliver—using a horde of the company's latest marvel, the 860

supermicroprocessor. By 1991, Intel plans to deliver a prototype of a "massively parallel" computer, dubbed Touchstone, that could contain as many as 2,000 of the 860 chips, each with the number-crunching power of a Cray-1. The prototype will probably have "only" 512 processors, but even that will set Intel back a cool \$20 million, since the Defense Advanced Research Projects Agency will chip in just \$7.6 million.

The computer will be engineered with flexibility in mind, says Justin Rattner, who heads the Touchstone project at Intel. For less number-intensive chores, Intel's upcoming 486 microprocessor could also be used in place of some 860 chips. By adjusting the number and mix of processors, he adds, "you can optimize the machine for specific problems and tasks."

HOW DETERGENTS MAY HELP WASH OUT BONE DISEASE

Detergent research may have pointed to a better treatment for osteoporosis, the debilitating bone disease that afflicts 24 million Americans, especially older women. Years ago, Procter & Gamble Co. discovered a drug called Didronel while studying diphosphonates for detergents. For a decade, Didronel has been used to treat a less-well-known bone illness called Paget's disease. But P&G's Norwich Eaton Pharmaceuticals Inc. has been researching other applications—and now has evidence that the substance can help bones to rebuild by blocking the agents that cause the bone loss of osteoporosis.

P&G has already asked for approval to market the drug for that purpose in Canada and six other countries, and within the next 12 months it expects to seek similar approval from the U.S. Food & Drug Administration. Results of large-scale clinical tests, due to conclude soon, seem to promise the hard evidence that will show Didronel's effectiveness.

STRIKING BACK AT CANCER'S PROTECTIVE PROTEIN

Doctors attack tumors with a whole battery of anticancer drugs. Combinations of drugs are used to knock out cancerous cells that may be resistant to some particular drug. But even when the initial treatment results in remission, some tumors grow back, especially with leukemia, ovarian cancer,

and breast cancer. When that happens, the tumor cells are usually resistant to many chemotherapeutic drugs.

Researchers now believe that multidrug resistance is the work of a protein called P-glycoprotein. In cancer cells, it acts as a magnet for chemotherapeutic drugs, removing them before they can affect the cell. Now, Centocor Inc., a Malvern (Pa.) biotech company, has developed a test based on monoclonal antibodies that spots P-glycoprotein. If the test, called P-glycoChek, can locate drug-resistant cancer cells, it may help determine the most effective tumor-fighting treatment. Even more important, the monoclonal antibody could be armed with radioactive compounds or drugs and home in on stubborn tumors with deadly accuracy.

A HEADREST THAT EMITS THE SOUNDS OF SILENCE

It's like an invisible driver's helmet that hushes annoying noises. In the headrest of the SilentSeat from Noise Cancellation Technologies Inc. are a microphone, speakers, and some sophisticated electronics. Any bothersome noises—the muffled roar of the engine in a truck, bus, or off-road vehicle, say, or a plane's propeller—are picked up, analyzed, and instantly negated by "antinoise." The speakers emit sound waves that are exactly the opposite of unwanted noise. Result: a blessed quiet that doesn't affect softer sounds, such as music or speech.



NCT President Michael J. Parrella says the technology is ready now. His New York City company is scouting for a trucking firm or fleet owner to place the first order. Initially, SilentSeats will cost about \$500 each, but once production gets going, the price would drop considerably, he adds. Beyond seats, NCT has developed an electronic car muffler and headphones that erase the din of machinery. One day, Parrella says, even windows in homes and apartments may sense vibrations from the outside and cancel them with antivibration in the glass, blocking the intrusion of urban noise.

THIS NEW PILL REALLY PUMPS OUT THE MEDICINE

Next time you take a time-release medication, you may be swallowing a pump as well. Inside a pill no bigger than some aspirin will be two compartments—one for a drug and on the other side of a flexible membrane, another containing a chemical with an affinity for water. In your stomach, the hydrophilic substance pulls fluid into the pill and swells up. It absorbs moisture. That pushes out spurts of medication through a tiny hole, one or two drops per hour.

Thus, patients who need a constant stream of medication can take just one of the so-called Oros pills, which could pump away all day long or until the pill passes out of the body. Developed by Alza Corp. in Palo Alto, Calif., the Oros system is already being used to deliver doses of an appetite suppressant, and Pfizer Inc. plans to use the new pill for its Procardia antihypertension drug. Alza claims the drug-release rate is affected by the relative acidity of a patient's digestive tract. As is the case with most time-release tablets and capsules. And the drug can be released slowly enough to avoid the side effects of many medications.

SmithKline Beckman

CORPORATION

has acquired

International Clinical Laboratories, Inc.

*Morgan Guaranty acted as financial advisor
to SmithKline Beckman and dealer manager
for the tender offer*

JPMorgan

JPMorgan

MEET THE WORLD'S BUSIEST MAN—OOPS, YOU MISSED HIM

Harunori Takahashi has an empire—and \$7 billion in debt

When real estate mogul Harunori Takahashi was deciding whether to buy a small Los Angeles office building last year, he invited California broker Michael D. Oh to dinner at an exclusive Tokyo restaurant. Oh arrived promptly at 8 p.m. and was ushered into a private room. About a half-hour later Takahashi breezed in, nibbled on the first course, chatted for a few minutes, and left. Another half-hour passed before Takahashi returned—only to leave again. Oh didn't know what to make of it. "Finally he comes in at around 11 and agrees to the deal," the broker recalls. "Then I realized what had happened: He had done three separate deals at the same restaurant in one night."

For Takahashi, it was business as usual. Juggling deals at a breathtaking pace, he has transformed the tiny Tokyo electronics company he took over 12 years ago into a conglomerate with assets estimated to be worth about \$7 billion. Through his privately held EIE International Corp., he owns a string of five-star hotels and resorts from Japan's Izu peninsula to Australia's Gold Coast (table).

Now, Takahashi, 43, is expanding his horizons. In January he announced plans to build the 46-story, \$300 million Regent of New York hotel on Manhattan's East 57th Street. EIE also intends to buy or build several more deluxe hotels in the U.S. and Europe. Takahashi is bidding for the Ramada Inc. hotel chain, and he's taking strategic stakes in several Pacific airlines to service his growing stable of swank resorts in Asia.

Although the high yen has spurred a tidal wave of Japanese investment over-

seas, few players have moved as swiftly and as aggressively as Takahashi. In just five years he has acquired more than \$3 billion worth of hotels, office buildings, and other foreign ventures. Among Japanese individuals who are heavy spenders abroad, only Shigeru Kobayashi of Shuwa Corp. has made as big a splash.

Yet Takahashi could be setting himself up for an equally dizzying fall.



TAKAHASHI: SOARING LAND VALUES UPPED HIS BORROWING POWER

Strong ties to a clutch of Japanese banks, notably Long-Term Credit Bank of Japan Ltd., have fueled his buying spree. But with an extraordinary \$7 billion in debt—roughly equal to his assets—he's walking a thin line. Some lenders want nothing to do with him. "We don't like the way he operates," says an executive at one of Japan's biggest banks. "He is way overborrowed."

EIE officials shrug off that concern. Robert Bungo Ishizaki, Takahashi's chief deal-spotter and unofficial ambassador, says he's confident that EIE could

comfortably double its borrowing even if interest rates edge higher because the value of many of its assets continue to climb. Junichi Hara, general manager of Long-Term Credit Bank's Shinjuku branch, is more circumspect but generally upbeat: "If future projects are of the same high quality, banks will be willing to participate."

HOW THICK? Some hotel experts think EIE may be aiming too high with its Regent of New York. With room rates averaging a staggering \$400 a night, the I. M. Pei-designed hotel is likely to be the city's most expensive when it opens in 1991. "There's definitely a market for a hotel like this, but there's some question about just how thick it is," says Stephen Brener, a New York hotel broker. An economic appraisal by Hospitality Valuation Services Inc. in Mineola, N.Y., however, assured Takahashi that the market is plenty big.

INSIDE EIE'S PORTFOLIO

Takahashi began amassing his fortune in 1977, taking over a troubled computer parts importer. Today he controls a diverse, \$7 billion empire. A sampling:

RESORTS LEISURE 25 resort hotels, including 7 Regents and 4 Hyatts, stretching from London to Australia; 2 golf courses, 6 more under construction

ELECTRONICS Stakes in 15 electronics companies, making everything from magnetic tape to portable phones

TRANSPORTATION TRAVEL Stakes in a shipping company, 2 air cargo lines, an aircraft leasing business, and a proposed, \$820 million Australian railway

OFFICE SPACE Prime downtown properties in Tokyo, Osaka, Hong Kong, Sydney, and Los Angeles

OTHER HOLDINGS Portions of four small Japanese financial institutions; 33% of an Australian gold mine

DATA: COMPANY REPORTS

Takahashi can move quickly because he eschews the lengthy consensus-building that prevails at most Japanese companies. In March, Ishizaki called for a meeting in Ho Chi Minh City. Although Takahashi had never been there, he promptly agreed. "It's better to make quick decisions because that will give you more time to do more business," he says.

Takahashi calls the shots from cramped offices on a side street in Tokyo's Ginza shopping district. Ishizaki, a Japanese-American, does most of

Why clients select J.P. Morgan for M&A.

1. Advice that is totally objective. Rather than promote merger and acquisition transactions simply to generate fees, we become a strategic financial advisor, bringing a relationship focus to a transactional business. If a transaction is not clearly in a client's best interests, we will recommend against it. Our clients expect and get from us objective advice, based on a thorough knowledge of their needs and goals.

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We've set our sights on being the world's leading M&A advisor, and that's why we're changing the way this business is done.

JPMorgan

People

globe-trotting, logging about 500 hours a year aloft in the company Boeing 727. The peripatetic investment adviser is bubbly and outgoing—a sharp contrast to Takahashi, who is uniformly described as quiet and unassuming. He has “no pretensions of grandeur,” says Michael A. G. Matthews, vice-president of Hong Kong-based Regent International Hotels, which EIE acquired 30% of in 1987.

‘NAUGHTY BOY.’ That quiet demeanor masks the drive of a go-getter. Wheeling and dealing is “a lot of fun,” says Takahashi. He works six days a week, from 9 a.m. until 11 p.m., and only unwinds on Sundays, with his wife, Shigeri, their two children, and his two dogs. He also enjoys golf, often playing with politician Shintaro Abe, a potential candidate for prime minister.

Takahashi may be an upstart in real estate circles, but he’s no rags-to-riches phenomenon. Born in Nagasaki Prefecture, the son of a film-company execu-



HYATT SANCTUARY COVE IS AMONG TAKAHASHI'S \$1 BILLION WORTH OF PROPERTY IN AUSTRALIA

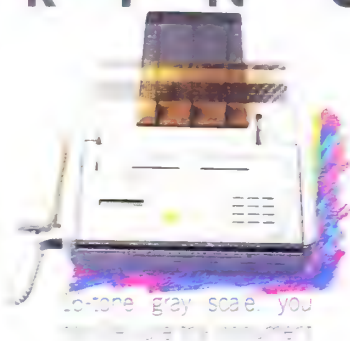
tive, he was raised in a large Western-style house with a swimming pool—a luxury in Japan even today. Flashes of Takahashi's determination showed in his youth. He was expelled from the prestigious Keio High School after he was caught selling tickets to a student-sponsored dance. That could have

wrecked his chances of getting into University, but he studied hard in a public school and was admitted. After graduating, he joined Japan Air Lines. There, Takahashi's ambition and life imagination won him the nickname “Warunori,” which translates roughly as “naughty boy.”



MITA BRINGING YOU

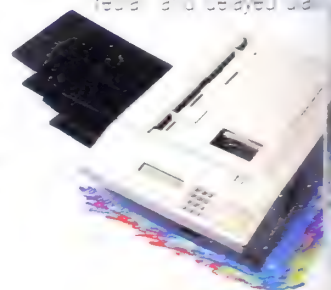
A Mita long distance copier, or fax machine, as some people prefer to call it, can reach out and send a copy to someone in as little as 15 seconds. Cross town. Cross country. Or across continents. At a cost is the price of a long distance call. And with a



teletypewriter, you send with the same crisp, clear copy quality. Mita is famous for

Of course all Mita long distance copiers come with a list of features as long as your arm. Take the high-volume TC-200, for example. It offers one-

touch dialing, automatic redial, and delayed dial-



he left JAL for EIE in 1977, at age 31. s founder, a friend of the Takahashi ily, wanted to retire but lacked an . When Takahashi stepped in, he d that the small importer of comput- elated products was saddled with ly \$8 million in debt. A lucky break e almost immediately, when the yen red. That slashed EIE's import bills, profits swelled. Takahashi then be- plowing those profits into central yo real estate, just before land prices he capital rocketed. Using his in- singly valuable property to secure k loans, Takahashi ventured abroad n the yen began to soar in 1985.

INTERSTROKE. He has made some t moves overseas, too. In 1987 he ght Hong Kong's Empress Hotel for million, cashing out a year later for million. At about the same time he \$16 million in cash and agreed to e \$200 million more for Bond Centre, ong Kong skyscraper that Austra- entrepreneur Alan Bond had just ght for \$243 million but couldn't fi- ce. The building, now 50% owned by ahashi, was recently valued at more \$770 million. EIE has also scored big Australia. Its more than \$1 billion th of property there, including the 0 million Hyatt Sanctuary Cove re- on the Gold Coast, makes Takahashi

one of that country's biggest foreign real estate owners.

As a leisure baron, Takahashi has plenty of home-grown competition. Lured by the surge in Japanese travel overseas, Japanese companies are rushing into the international hotel and resort business. In 1987, Aoki Corp., together with Robert M. Bass Group Inc., paid \$1.4 billion for Westin Hotel Co. Last fall, Seibu Saison Group snagged

Takahashi's \$300 million Regent of New York, opening in 1991, will have rooms averaging \$400 a night

InterContinental Hotels Corp. for \$2.3 billion. And Tokyu Corp., a retailing conglomerate, owns 16 vacation complexes.

Takahashi's response: speedy expansion of his South Pacific leisure portfolio. EIE is buying or building about 10 more hotels in Bali, Guam, and other tropical locales. It is also poised to take 10% stakes in Air Caledonie and Air Pacific, the Fijian national carrier. A source close to EIE says it will soon buy a 50%

interest in state-organized Air Saigon, which will service newly opened vacation spots in Vietnam. And now Takahashi is heading west. He's preparing to buy or build hotels for the Regent chain in San Francisco, London, Istanbul, and several other U.S. and European cities. All will cater to business travelers.

The big question hanging over EIE, however, is whether it can pay its shopping bills. Just in case lenders suddenly get cold feet, EIE is learning the art of creative financing. Working with Drexel Burnham Lambert Inc., it will soon issue \$100 million of nonrecourse, high-yield notes in a private placement to fund its purchase of three Tahiti hotels.

Nonrecourse financing, which shields the issuer in the event of a business failure, is common in U.S. real estate circles but rare in Japan. "It's a smart move, but it's risky because the interest cost tends to be much higher than normal bank financing," says one Japanese investment banker. Such warnings shouldn't faze Takahashi, though. For a man who leapfrogs through three-deal dinners, calculated gambles are what make the game so much fun.

By Amy Borrus in Tokyo, with Dori Jones Yang in Hong Kong, Stephen Hutcheon in Sydney, and Peter Finch in New York



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FIDELITY FIGHTS

CAN CEO JOHNSON REVIVE THE BEHEMOTH OF THE MUTU



NED JOHNSON'S EMPIRE

FIDELITY INVESTMENTS-RETAIL

Mutual fund company, with \$48 billion in assets under management. Includes 173 funds

FIDELITY INVESTMENTS-INSTITUTIONAL

Institutional money manager, overseeing \$40 billion in 401(k) plans, pension and trust funds

FIDELITY BROKERAGE SERVICES

Nation's second-largest discount broker, with 55 branch offices handling 1.7 million accounts offered through banks and

At Fidelity, the nation's largest mutual fund group, the numbers for 1988 have just come out, and they are bad. In the first full year since the stock market crash, revenues were down by one-quarter and profits plummeted 70%. But Fidelity Chief Executive Officer Edward C. "Ned" Johnson III is unperturbed. Relaxing in his modest fifth-floor office in downtown Boston, decorated with large Chinese vases and an oil painting of Canton harbor, he is almost mad-deningly serene as he contemplates the year gone by. "It is a horrible thing to say," Johnson says, "but it may have been good for us. We were getting fat and happy."

Such a remark would seem impudent coming from the typical company executive who must explain poor operating results to an army of disgruntled shareholders. But the 58-year-old Johnson is no typical executive, and there is no army of

shareholders, disgruntled or otherwise. Johnson is the undisputed ruler of a privately held financial service empire whose stock, bond, and money-market funds, discount brokerage, and pension fund operations encompass 2.3 million customer accounts—putting it in the same league as Merrill Lynch, Citicorp, American Express, and other financial service leaders. But no CEO of any comparable company is as powerful—and independent. This little-known, unconventional executive will find his stewardship of Fidelity severely tested in the months ahead.

DECEPTIVE PROFILE. With his Boston Brahmin background and contemplative personality, Johnson doesn't fit the mold of the tough, streetwise executive. By the egomaniacal standards of Wall Street, he is gentle, unpretentious, and publicity-shy. But don't let that fool you. Johnson is a fighter. And with good reason: He and his family own a 47% interest in Fidelity,

worth about \$1 billion, giving Johnson an unusually large stake in the future of the company.

Johnson is battling on a number of fronts. He has cut personnel by almost a third, from a precrash high of 8,100 employees—a far more severe retrenchment than has been endured by any Wall Street firm. With staffing levels trimmed to better ride out the market uncertainty, Johnson is putting the company in fighting trim for the next bull market. While he has held back from introducing many new funds, he is beefing up Fidelity's discount brokerage in a bold gamble that the small investor will return to the market en masse. He is hedging his wager on the short-term stock players by strengthening Fidelity's fast-growing institutional operation, building on the company's position as the largest manager of 401(k) retirement savings plans. Fidelity's 20-year-old foreign presence is being sharpened, and Johnson

BACK ID INDUSTRY?

HANDS-ON MANAGER:
JOHNSON IN THE BATTERY
ROOM, WHICH PROVIDES
BACKUP POWER FOR
COMPUTER OPERATIONS

INTERNATIONAL

mutual fund company, billion in assets; offices in Tokyo, Taipei, Sydney, Hong Kong

FIDELITY PROPERTIES

Real estate company that owns 12 buildings, including the Boston World Trade Center, and restores old properties

FIDELITY INVESTMENT LIFE INSURANCE CO.

Insurance company, in joint venture with Monarch Capital to sell investment products

FIDELITY VENTURE ASSOCIATES

Venture capital company, with \$20 million invested in startups and leveraged buyouts, \$75 million under management

so applying more resources to the potentially lucrative field of insurance. Advertising, slashed in 1988, is being increased, with much of the marketing push now devoted to retirement products.

At Johnson's most powerful asset is Fidelity's reputation. The company has an annual of mutual funds that have shown impressive returns. The largest and most successful of them is Magellan (table, page 69). While cash is no longer cascading into Fidelity's equity funds at anywhere near precrash rate, customer assets are nevertheless being built up steadily. Much cash is flowing into the company's money market mutual funds, poised for the day when stocks come back into favor. In the mutual fund industry, the clear trend is to recapture money in the short-term end of the market," notes Avi Nachman, an analyst with Strategic Insight, a mutual fund research company. "When there have more than \$80 billion under man-

agement and have the No. 1 fund manager in the business, you can take more chances."

So far this year, overall investor interest appears to be picking up. According to the company, customer inquiries in March were up 20% from the year before, while new equity accounts were up 30%. And since January, sales have exceeded redemptions.

SECTOR PIONEER. The nerve center of Fidelity's operations is housed atop a refurbished pier in a vast, colorfully decorated building with a stunning view of the Boston skyline. Inside, hundreds of marketing and service employees sit before computers and a small robotic cart wheels around dropping off and picking up mail. Here is where the paperwork is handled for Fidelity's 173 mutual funds, from the pint-size Capital Goods and Industrial Materials sector funds, managed by Johnson's daughter and possible successor,

Abby, to the \$10 billion Magellan Fund. The other major subsidiaries—the discount brokerage, institutional investment, and foreign operations—have their offices at other locations in Boston.

During the bull market Fidelity became the very embodiment of the mutual fund, its advertisements featured in almost every financial publication and business section. Fidelity catered to the growing enthusiasm for funds by pioneering sector funds, with superspecialized portfolios. It also introduced "telephone switching," allowing customers to change funds easily. From 1983 to 1987, assets under management multiplied fourfold, to \$75 billion, while revenues and earnings quadrupled (charts, page 70). But Bloody Monday put an end to all this unrestrained growth. The newly released 1988 results for FMR Corp., Fidelity's holding company, show that revenues declined to \$870 million, from \$1.08 billion in 1987, and that profits

plummeted to \$24 million, from \$80.7 million—the lowest level since 1984.

As the proprietor of a private company, unburdened by the need to produce quarterly financial progress, Johnson can live with lackluster profits as he builds for the future. He was reared by a father who foresaw the long-run potential of mutual funds back when they were an esoteric investment. Edward C. Johnson II was an attorney who bought the \$4 million Fidelity Fund in 1946 and went on to become a legend on Wall Street by building it into a business with \$4 billion in assets. The elder Johnson had a philosophical bent, frequently peppering his dissertations on the market with references to Chinese and Zen Buddhist philosophers to try to explain market behavior.

TSAI GRAD. By all accounts, Ned was a precocious young fellow. Elsie Mitchell, his older sister, recalls the time when, as a 12-year-old, Ned rigged up an electronic eye outside his bedroom. When the gadget was set off, it would open his door, turn on the lights, and start the radio playing. That foreshadowed his adult fascination with all things mechanical. But Ned didn't expect to make his living fixing toasters. His ninth-grade English teacher at the Milton Academy, Johnston Torney, recalls one occasion when he criticized Ned's poor spelling. Ned retorted that he didn't have to learn to spell correctly—be-

HOW FIDELITY'S LARGEST FUNDS HAVE FARED

Fund	Net assets (4/3/89) Billions	Annualized total return*		
		1988	Three-year	Five-year
MAGELLAN	\$9.68	22.76%	11.13%	21.06%
EQUITY-INCOME	4.46	22.49	9.73	16.62
PURITAN	4.43	18.89	9.78	16.68
HIGH INCOME	1.83	12.59	8.09	13.46
CAPITAL APPRECIATION	1.82	37.62	NA	NA
HIGH YIELD MUNICIPAL	1.58	12.22	6.18	11.20
DESTINY I	1.55	19.48	10.70	18.38
FREEDOM	1.27	15.53	8.84	17.07
GROWTH & INCOME	1.21	22.98	13.61	NA
OVERSEAS	1.06	8.26	17.25	NA
S&P 500		16.51	10.94	17.40

*Includes reinvested dividends and capital gains; three- and five-year numbers are as of March 31
NA = not applicable
DATA: MORNINGSTAR INC.

cause he would always have a secretary.

After graduating from Harvard in 1957, Johnson served in the Army and then worked at State Street Bank before joining his father's company. At Fidelity he was trained by none other than Gerald Tsai, then the boy wonder of the investment world. The two soon became rivals, but it was never in doubt who would prevail—even though Tsai was a favorite of the elder Johnson and was allowed to acquire 19% of the company. Eventually Tsai, frustrated by his inability to rise to CEO, cashed in his stake and left.

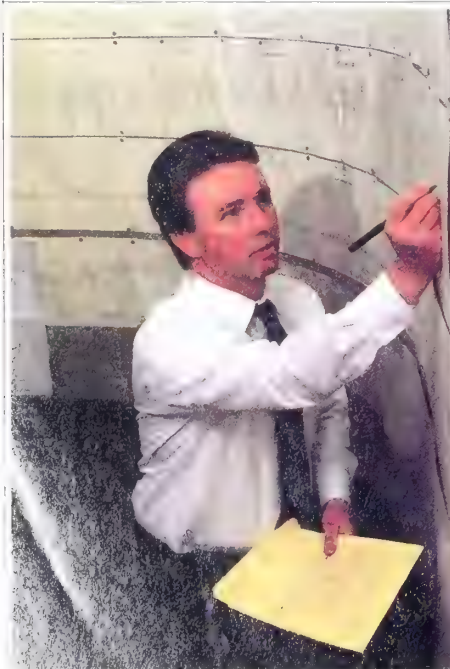
As Ned Johnson took over the business in 1972, it soon became evident that he was no mirror image of his father. If "Mr. Johnson" was drawn to the mysteries of Zen, Ned became a devotee of Japanese-style management. He began by integrat-

ing the company vertically, taking over the back-office account-processing functions from the banks to handle the job for most mutual funds and dropping sales through brokers in favor of direct sales.

CAB STAB. With the entire process under his control, he was able to swiftly add new products. Whereas his father stuck to mutual funds, the son yearned to enter new businesses. "The Japanese try a lot of new things," Ned Johnson notes. "They [sometimes] get their heads handed to them, but they keep learning."

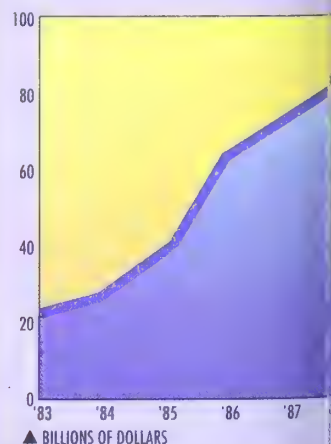
Some of Johnson's ventures were out of the financial orbit, such as the car service he began in 1985 after having trouble flagging a cab or the executive search firm and employment agency he also started. The successes tended to outweigh the failures. One of the biggest hits, pioneered by Johnson in 1981, was a line of industry-specific sector funds that enable investors to switch from industry to industry.

While the old Fidelity was a small money-management organization, the new Fidelity included thousands of market and service people working on phones and computers. Johnson has tried to instill among them a Japanese-style sense of corporate identity. He aggressively solicits suggestions and meets new employees—be they fund managers or carpenters—at cozy tea parties in a director's room around a gleaming walnut table.



PLOTTING TRADING
TRENDS IN
FIDELITY'S
CHART ROOM

FIDELITY IS MANAGING MORE MONEY...



at despite all the surface
gality, Johnson does not
by consensus. Many of
key decisions, including
in 1979 to build a dis-
at-brokerage business,
made against the advice
is senior managers. He
maintained direct operat-
control while granting a
deal of independence to
managers by spinning off
sions into 20 separate
idiaries, the presidents
hich generally report di-
y to him. The goal is
short-term profits but
with. "When you meet
him, you don't talk bud-
" says John J. Cook Jr.,
dent of Fidelity Manage-
Trust Co. "The penalty
Fidelity is if you don't
rate."

VU. The question facing
company is whether it
continue to thrive by in-
ting, which worked so well during
free-spending euphoria of the bull
et. "We've been through a hell of a
orse," Johnson insists. Indeed, when
ook command of Fidelity in 1972, it
in the midst of a slumbering market.
ng his first two years in office, assets
nk 30%. Johnson had to resort to the
slip—lifetime employment being one
nese custom he has yet to embrace.
though he has tightened Fidelity's
retrenchment runs counter to John-
free-spending style. "Johnson is a
er, not a caretaker," says Roger T.
son, a senior vice-president who
s Fidelity's new businesses. "We are
t at managing growth. People here



**'Johnson is a builder, not a caretaker. . . .
People here don't get their
kicks out of laid-back management.'**

ROGER T. SERVISION
*Senior vice-president
of Fidelity*

don't get their kicks out of laid back man-
agement." Indeed, at a time when most
U. S. financial companies are cutting back
their costly foreign operations, Fidelity is
trying to create an international financial
supermarket. Fidelity International—
which Johnson established in 1968, with a
base in Bermuda as a way of attracting
foreign investments—already has a large
overseas presence. Since becoming inde-
pendent from the U. S. holding company
in 1980, its mutual fund and pension as-
sets have quintupled, to \$10 billion. Now
the foreign operation is reuniting with its
U. S. cousin in a joint venture that will
double to 50 the number of its internation-
al analysts.

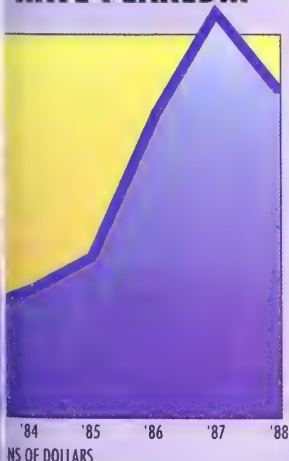
With offshore equity mar-
kets now twice the size of the
U. S. stock market, says J.
Gary Burkhead, president of
FMR, "we could end up with
our international research op-
eration larger than the U. S.
operation." Fidelity in March
dispatched Richard Haber-
mann, head of domestic re-
search, to London to take
charge of the overseas re-
search unit.

CAPTIVE MARKET. Fidelity is
also hotly pursuing institu-
tional business. After a peri-
od of poor performance, Fi-
delity reorganized its pension
business in 1981 to draw
more heavily on its star fund
managers. Fidelity also went
after 401(k) retirement sav-
ings plans, becoming the
largest manager of 401(k)s.
Institutional assets under
management quadrupled
from \$9.9 billion in 1984,

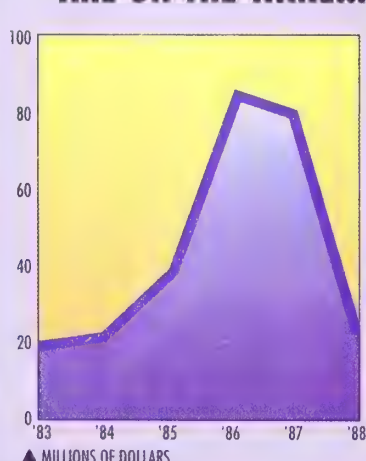
when they were about 36% of total assets,
to \$40 billion, now 46% of assets. Pension
fund assets alone surged from \$5.4 billion
in 1987 to \$8.5 billion last year.

Johnson is also moving Fidelity into the
insurance business. FMR has already pur-
chased a small Philadelphia insurance
company and is offering to Fidelity's ex-
isting customers, in states where it has li-
censes to sell insurance, investment prod-
ucts such as single-premium policies,
deferred annuities, and variable life poli-
cies. Where Fidelity does not have a li-
cense to operate, it is selling the products
of Monarch Capital Corp., with which it
has a joint venture. Fidelity has the ad-
vantage of a captive market. "It's one-

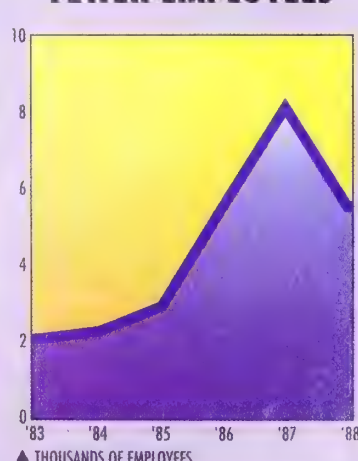
BUT REVENUES HAVE PEAKED...



...PROFITS ARE ON THE WANE...



...AND THERE ARE FEWER EMPLOYEES



tenth the cost to sell to existing customers," says Servison. Fidelity plans to spend \$50 million to \$100 million to develop its insurance products over the next five years.

Johnson plans to expand Fidelity's discount-brokerage operation, already the second- or third-largest in the nation (Quick & Reilly Group Inc. also claims the No. 2 spot) after Charles Schwab Corp. Although Fidelity has closed four offices since the crash, it has opened three new ones and plans to keep adding 5 to 10 a year and to acquire smaller discount brokers. Fidelity hopes to boost trading volume by selling more of its Investor's Express product. It's a service that allows customers to do their own stock trades through their home personal computers—so-called desktop investing. The product attracts particularly active traders who generate a lot of business for Fidelity.

With the advertising budget being gradually increased—Fidelity won't say by how much—the company is concentrating on marketing its retirement investments. Much of that advertising is done through the company's 32-page glossy magazine, *Investment Vision*, which is sent to customers and recently had an article on its Keogh, IRA, and variable-life products used for retirement.

PAYING THE PIPER. Another area being given special emphasis is computer software—in line with Johnson's practice of making small, undramatic improvements as a way of increasing long-term profitability. Among other equipment, Fidelity will soon purchase some 1,000 new PCs to run software the company has developed that will enable telephone representatives to tap more information and respond more quickly to customer requests. "Our competitors who don't have these [software] skills will be paying a far bigger price 5 to 10 years from now," says Johnson.

Once committed to something, Johnson can be relentless. At work, his idea of fun is camping out at the office for several days at a time trying to learn how a new computer system works or taking apart a new automatic check-scanning device and suggesting modifications—practices colleagues say can drive them bananas. "It is obviously not what I am paid for," Johnson admits, "but there has to be a certain amount of time for frivolity."

Johnson's yen to spend worries observers. "Eventually the investor is going to

have to pay for all that," says Eric Kobren, who writes a newsletter that follows Fidelity mutual funds. Since the crash, Fidelity has in fact gradually boosted its various fees and added sales charges. And it's facing stiff price competition. John Bogle, CEO of Vanguard, a venerable competitor in the mutual fund business, claims that the Fidelity investor pays an average of \$15 for every \$1,000 invested, slightly higher than the average among no-load funds and more than three times what the Vanguard investor pays. (Fidelity asserts that its overall expense ratio is just 0.657%, vs. a fund-industry average of 0.72%. However, Fidelity's numbers do not include sales charges.)

The company recently came out with



'The Japanese try a lot of new things. They [sometimes] get their heads handed to them, but they keep learning.'

EDWARD C. JOHNSON III
Chairman and CEO
of FMR Corp.

the Spartan Fund, which offers a low expense charge for larger, less active investors. The product has done well, but it has cannibalized business from the higher-margin products. Johnson's stress on innovation has also drained resources. "He could improve profitability more by growing less and experimenting less," says A. Michael Lipper, chairman of Lipper Analytical Services Corp.

Morale has suffered as a result of the layoffs, a setback for Johnson's efforts to develop company loyalty. And although he has succeeded in retaining Fidelity's most visible fund manager, Peter Lynch (box), the company is otherwise losing some key people. The highest officer to leave recently was John F. O'Brien, who left his post as group managing director at the end of March. Like Tsai, O'Brien says he was frustrated that he could never run Fidelity.

Despite these problems, Johnson has managed to hold his own against the competition. Although Fidelity's profit plunge is more comparable to discount broker

Charles Schwab's 70% decline in profit than to mutual fund rival Dreyfus' drop, Johnson can take comfort in knowing he has maintained market share. Fidelity says its portion of total U.S. mutual fund assets has grown slightly since the crash, to 9.25%, while Merrill Lynch and American Express Co., the two other largest operators of mutual funds, have both suffered a slight decline in their share of assets, to less than 8.5%.

Fidelity has also made good money from investments in venture capital and Boston real estate that Johnson bought in the early 1970s for a fraction of its current value. "We have probably made much more money on our capital as we have on our regular business," he says. Still, Johnson admits that operating profits must be increased over the long term: "No one will stay here unless they are well paid, and no one will be well paid unless they make a very good profit."

Actually, there's more to it than that. Of the top 10 employees, 280 have been allowed to buy Fidelity stock at book value, which has been rising for many years through 1987. If they leave, they must sell the shares at book value. If they stay, however, and Fidelity goes public, as many believe eventually will, they stand to gain an immediate 50% to 1,000% on their shares. Lynch, a large shareholder, says that possibility helps to retain good fund managers.

Were the company to go public, market value is conservatively estimated to be in the neighborhood of \$1 billion.

Johnson discounts the possibility that Fidelity will go public under his rule, however. Like his father before him, Johnson feels strongly about keeping the company private, preferably in the family. At present, there appears to be no ready successor within the clan. One of his two daughters, Abby Johnson, just started running a small fund last January. His only son, Edward Johnson IV, of college age, is a member of a ski patrol in Vermont and has yet to show an interest in the business.

In any event, succession is the least of Johnson's worries. So long as the market remains in the doldrums, he will have a fight on his hands. And whether he wins or loses, the person most deeply affected will be the man to whom Ned Johnson is accountable—Ned Johnson.

By Leslie Helm in Boston, with
Friedman and Gary Weiss in New York

JOHNSON AND LYNCH: AN ODD COUPLE WITH A HIT FORMULA

Peter Lynch, manager of the \$8.68 billion Magellan mutual fund, is a rarity at Fidelity Management & Research Co. And not just because he runs the nation's largest in the past 10 years, best-performance mutual fund. Among the ranks of some Fidelity portfolio managers, a star. And in an industry where are invariably shunted into management, Lynch remains in the trenches, happily. "All I ever wanted to do was run a mutual fund," says the 45-year-old. "I don't have to spend any time worrying about Fidelity's company."

In his battle to shore up Fidelity against the tide that has infected mutual funds, Fidelity chairman Edward C. Johnson III can't count on having Lynch in the corner. Johnson and Lynch's relationship is extraordinarily stable by the volatile norms of the securities industry, where many firms have been ravaged by the publicized exits of top producers. "I would think that either of them would let problems get in the way," says a former Fidelity executive. "But apparently there is no problem."

SELLER. Lynch's career has paralleled the growth of Magellan, which he has managed since 1977. During the years that ended in 1991, Magellan scored an average annual gain of 11% vs. 17.4% for the Standard & Poor's 500-stock index, and in 1988 it returned 22.7% vs. 16.5% for the S&P. The fund is now gargantuan—it has 1,400 stocks—and Lynch is much sought after as a stock market guru. "He is the only person from Fidelity I hear about regularly," says Rich Dunne, producer of the *Wall Street* television program. Lynch has also led an investment primer, *One Up Wall Street*. Published in February, the 80,000 copies are in print—high to put it on *The New York Times* best-seller list for advice books. In their contrasting personalities, Johnson and Lynch make for an odd

couple. Johnson is regarded as an introvert, while Lynch is outgoing and witty. He seems to enjoy the give-and-take of dealing with the media. At Fidelity, Johnson is clearly the boss, but he doesn't second-guess Lynch's investment picks. In fact, Lynch says he speaks with Johnson "only a couple of times a year." Johnson provides the facilities and, more important, "the culture that lets him do his work," says A. Michael Lipper, head of Lipper Analytical Securities Corp.

"It's like the San Francisco Forty-Niners: Peter is Joe Montana, a great

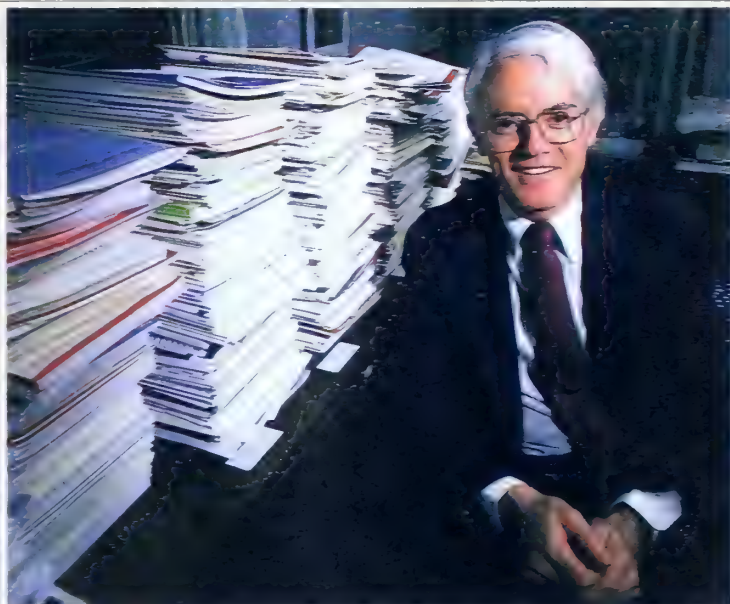
decades of service. In recent years, mortgage-backed securities guru Lewis S. Ranieri left Salomon Brothers Inc. because he clashed with Chairman John H. Gutfreund. Likewise, merger maestros Bruce Wasserstein and Joseph R. Perella fled from First Boston Corp. because of differences over the company's direction.

NO MR. NICHE GUY. Lynch considers Fidelity home. After graduating from Boston College and receiving an MBA from the Wharton school of finance, he served two years in the army. He has spent his entire 20-year career at Fidelity. After his first year a \$1,000 raise brought his annual salary to \$17,000. At that time, Lynch was offered \$55,000 a year to manage money for a New York brokerage. For a man who was recently married and wanted to start a family, it was awfully tempting—but he turned it down. "The problem with Wall Street is, you get into a very narrow niche," Lynch explains. "You tend to become an expert in only one field." In the end, Lynch turned out all right: His salary is now estimated at \$8 million to \$9 million a year. Lynch has become Fidelity's second-largest stockholder, with a 5% ownership. He, his wife Carolyn, and their three daughters live in a sea-side Boston suburb.

It's clear that Lynch respects Johnson. "Ned's determination is one of his most notable traits," says Lynch. "I'd hate to be a sumo wrestler in the ring with him. He'd push you out, somehow." But Johnson probably wouldn't ruffle Lynch, either. "For his visibility, his continuity, and his record, he is stunningly important to Fidelity," says Jack Sullivan, a partner at Van Kasper & Co.

And so he will be—as long as Magellan continues to shine. If it slips, Lynch's fame won't be of any help. Indeed, Johnson describes Lynch's celebrity status as a "two-edged sword. As long as he performs well, it's fine."

By Jon Friedman, with Leslie Helm, in Boston



"All I ever wanted to do was run a mutual fund. I don't have to spend 1% of my time worrying about Fidelity, the company."

PETER LYNCH
Manager
Fidelity Magellan

on-the-field player who has an ability to score points dramatically. Johnson is like Bill Walsh," the acclaimed coach who retired in January after the Forty-Niners won their third Super Bowl. In Johnson's system at Fidelity, Lipper notes, Lynch can flourish, just as Walsh brings out the best in his quarterback Montana.

Johnson has resisted installing Lynch in the executive suite. The Fidelity chairman notes that it would be "an incredible waste of talent if someone is good at running money to put him in management." Wall Street is littered with superstars who eventually opposed their bosses and departed after

BIG RETURNS IN SMALL PACKAGES

Tiny funds were the first quarter's titans—many by betting on little stocks

History proves that over the long haul, a diversified portfolio of small-company stocks does better than one made up of blue chips. But for most of the bull market of the 1980s, big names were the best performers. Returns from small-company issues—and the mutual funds that invested in them—were anemic. After the 1987 crash, however, investors rediscovered small stocks. And in the first quarter of 1989, small funds that invested in small stocks were some of the biggest winners.

Take the top-performing Alger Small Capitalization Fund, up 20.21%. After a knockout quarter, it still has only \$4.3 million in assets. "We've had virtually no new cash come into the fund in the last quarter," says portfolio manager David Alger. Few people even know the fund exists. It only recently rounded up the 1,000 shareholders needed to merit inclusion in the fund listings in the daily newspaper. The Kaufmann Fund, No. 2 in the quarter and tops for 1988, has more than doubled in size since yearend, yet holds just \$12.2 million in assets. In fact, the only fund of any size in the top 10 is No. 4—Twentieth Century Ultra, with about \$290 million in assets. The combined assets of the other nine total only about \$200 million. And of the top 50 funds, only two have more than \$500 million: Scudder Capital Growth, with \$600 million, and Twentieth Century Growth, with \$1.27 billion.

GOLIATHS THAT GAINED. Although small was profitable over the winter months, big funds didn't exactly freeze up. The behemoth Fidelity Magellan Fund, with \$9.67 billion in assets, racked up a 9.52% total return (table). In all, 3 of the 10 largest funds beat the 7.13% return of the Standard & Poor's 500-stock index. Seven of the 10 beat the 6.22% equity-fund average calculated by Morningstar

Inc., which tracks 849 such funds.

The inflation fears that ran rampant through the stock market in the past few weeks were mirrored in the mutual funds. Rising oil prices propelled some funds specializing in natural resources into the ranks of the top 50 performers. Gold funds, often key performers when inflationary winds blow, averaged gains

Perhaps the biggest disappointment for fund investors in the first quarter were the international funds, especially those that invest in Japan. That sounds crazy, since the Nikkei stock average zoomed 8.9% in that time. But remember: The funds are priced in dollars, not yen, and the yen dropped 8% against the greenback, which largely wiped

gains for dollar-based investors. **SHREWD MOVES.** But in different investment climates, smart moves can pay off. Christian Wignall, who runs the G.T. Japan Growth Fund, scored an impressive 15.42% return by making a few shrewd moves. While most Japanese funds try to match the market, the Tokyo market, Wignall overweighted the fund with steel, construction, and trading-company stocks. They all did well. And he held few financial stocks, which were relatively poor performers. But savvy stock selection in a foreign fund can be undercut by an adverse shift in currency.

Wignall offset his currency exposure by hedging the portfolio against the falling yen. He doesn't always pay for that expense, but he thought rising interest rates in the U.S.

would cause the dollar to appreciate against the yen. In mid-March, as much as 74% of the portfolio was hedged, but he has since scaled back in anticipation of a resurgence in the yen.

As for the Tokyo market, Wignall is still bullish—but is rejiggering the portfolio to load up on electronics and small-cap stocks.

Buying a small fund that invests in small companies is, in itself, no guarantee of investment success. The portfolio manager still has to choose the right stocks. The winning managers cited investments in cellular-telephone, entertainment, specialty-retailing, and health care stocks as reasons for their shining performances.

The biggest winners steered clear of high-tech stocks. That's no easy feat

HOW THE LARGEST FUNDS PERFORMED

Fund	Assets Billions	Total return*
FIDELITY MAGELLAN	\$9.68**	9.52%
WINDSOR	6.79	6.89
FIDELITY PURITAN	4.43**	5.89
INVEST. CO. OF AMERICA	4.29†	6.90
FIDELITY EQUITY-INCOME	4.46**	7.48
TEMPLETON WORLD	4.16	6.78
PIONEER II	3.92	7.12
AFFILIATED	3.32	3.80
WASHINGTON MUTUAL INV.	2.95†	7.21
AMERICAN MUTUAL	2.65†	5.80

*Appreciation plus reinvestment of dividends and capital gains, Jan. 1-Mar. 31, 1989 **As of Apr. 3 †As of Mar. 1
DATA: MORNINGSTAR INC., BW



of 4.65%. Still, they did better than gold bullion, which dropped 7.74%. One outstanding gold fund was United Services Gold Shares, up 14.67%. Portfolio manager Edmund Serfaty credits the performance to a surge in South African gold shares. Many precious-metals funds either minimize or exclude South African stocks. That may have kept them out of the winner's circle.

small-cap universe heavily populated by those gee-whiz companies. Computer stocks in particular have gone downhill since mid-February, with IBM and Digital Equipment down the line. Investors are led by the way the big computer companies have begun to dampen expectations for their earnings. Many funds utilizing in technology sank to the bottom 50 of the quarter's lineup.

NO EDGE. The impact of a few win-stocks on a small portfolio can be enormous, especially in the quarter-to-quarter performance derby. Funds with assets of millions in assets may have added a few stocks, so even a few big winners don't necessarily make much of a difference. But for small funds with, say, assets of millions, a few big gains can provide a real boost.

Like the Alger Small Capitalization Fund, the Founders Frontier funds owned shares in FHP International Corp., a California health-maintenance organization that went up over 80% in the first quarter. The fund also owned stock in Windmere, a maker of personal-care products, which climbed nearly 50%. Kaufman's big gainer was POP Radio Corp., a fast-growing company that provides services with background music laced

The biggest winners steered clear of high-tech stocks and reaped rewards in health care and entertainment

advertising. It was up 67%. And the Delaware Group Trend Fund enjoyed a big rise in price of its prize holding, the Film Entertainment Inc. "It's a lovely company with good talent, discipline, and finances," says portfolio manager Edward Antonian.

In small funds, the question of whether the portfolio manager is a stock-picker or just lucky is even more critical than it is with large funds. In larger, well-diversified funds, market movements usually have more influence on returns. In small funds, however, stock movements can quickly magnify or diminish returns. The 44 Wall Street Fund, while not a quarterly winner, managed to return an average of 27.6% a year during the bull market.

Still, that's no reason to shun small-cap funds. It looks as if such funds are out of favor for nearly five years, but they are pulling ahead of the bigger funds. By Wall Street's reckoning, a trend that, once in place, is likely to last for several years to come.

by Jeffrey M. Laderman in New York

EQUITY FUNDS: THE BEST AND WORST OF THE FIRST QUARTER

LEADERS	
Fund	Total return*
Alger Small Capitalization	+ 20.21%
Kaufmann	18.92
Delaware Group Trend	18.36
Twentieth Century Ultra Investors	18.13
Fidelity Select Medical Delivery	17.45
Founders Frontier	17.32
Lehman Capital	17.07
Fidelity Select Broadcast & Media	16.95
Fidelity Select Air Transportation	16.94
Fidelity Select Regional Banks	16.83
Scudder Capital Growth	16.37
AARP Capital Growth	16.14
Financial Strategic Health Sciences	15.77
G.T. Japan Growth	15.42
Quasar Associates	15.01
United Services Gold Shares	14.67
Retirement Planning Equity	14.64
Afuture	14.64
Fidelity Select Energy Service	14.10
Flag Investors Emerging Growth	14.09
Twentieth Century Vista Investors	14.07
Legg Mason Special Investment	14.07
Financial Strategic Leisure	13.99
Fidelity Select Biotechnology	13.96
Wealth Monitors	13.93
Founders Special	13.71
Carnegie-Cappiello Total Return	13.38
Vanguard Specialized Energy	13.35
T. Rowe Price New America Growth	13.33
G.T. Pacific Growth	13.27
Surveyor	13.13
Alliance Global Canadian	12.99
Hartwell Growth	12.97
Fidelity Select Telecommunications	12.97
National Aviation & Technology	12.90
American Investors Growth	12.83
Putnam Information Sciences	12.74
Fidelity Select Financial Services	12.57
Shearson Lehman Hutton Aggr. Growth	12.53
American Telecommunications Growth	12.38
Carnegie-Cappiello Growth	12.35
Gabelli Asset	12.25
ABT Investment Emerging Growth	12.14
Financial Strategic Energy	12.12
Fidelity Select Energy	11.98
Century Shares	11.97
Twentieth Century Growth Investors	11.94
IDEX	11.89
Stein Roe Discovery	11.88
Janus	11.86

LAGGARDS	
Fund	Total return*
Fairfield	-4.62%
Alliance Technology	-4.37
Merrill Lynch Pacific A	-4.10
Van Eck World Trends	-3.17
Security Omni	-2.87
Japan	-2.33
Fidelity Select Paper & Forest	-1.90
Keystone International	-1.87
Nomura Pacific Basin	-1.44
Flex-Fund Income & Growth	-1.20
Fidelity Select Computers	-0.95
Sigma World	-0.88
Colonial International Equity Index	-0.82
International Equity	-0.50
Franklin Utilities	-0.33
Rochester Growth	-0.29
Permanent Portfolio	-0.13
Vanguard World International Growth	-0.10
IDS International	0.00
Shearson Lehman Hutton Sp. Inc. Util.	0.00
Fidelity Select Software & Computer	0.14
Shearson Lehman Hutton Global Equity	0.36
Fidelity Select Industrial Materials	0.38
Prudential-Bache Global	0.40
Oppenheimer Premium Income	0.42
Dreyfus Leverage	0.44
IDS Strategy Pan Pacific	0.46
Scudder Gold	0.63
Sci/Tech Holdings A	0.63
Fidelity Utilities Income	0.74
Loomis-Sayles Capital Development	0.76
Fidelity Select Electric Utilities	0.76
John Hancock World Pacific Basin	0.83
National Real Estate Income	0.85
IRI Stock	0.88
Merrill Lynch Eurofund B	0.91
ISI Growth	0.92
MFS Lifetime Global Equity	0.92
American Heritage	0.93
Blanchard Precious Metals	0.95
Strategic Gold/Minerals	1.00
Dean Witter Utilities	1.16
Dreyfus Capital Value	1.19
Environmental Awareness	1.26
Rodney Square International Equity	1.26
IAI International	1.29
National Growth	1.33
Fidelity Select Electronics	1.34
Meeschaert Capital Accumulation	1.39
John Hancock Global	1.44

S&P 500-STOCK INDEX 7.13
EQUITY FUND AVERAGE 6.22

*Appreciation plus reinvestment of dividends and capital gains, Jan. 1-Mar. 31, 1989

DATA: MORNINGSTAR INC.

BY GENE G. MARCIAL

CAN YOU BUY INSURANCE AGAINST A RECESSION?

What kind of advice are the nation's large pension-fund managers getting these days? If they listen to Bailard Biehl & Kaiser in San Mateo, Calif., whose clients manage \$75 billion, the asset-allocation message is clear: "Bail out of most stocks fast—and buy insurance." Insurance stocks, that is.

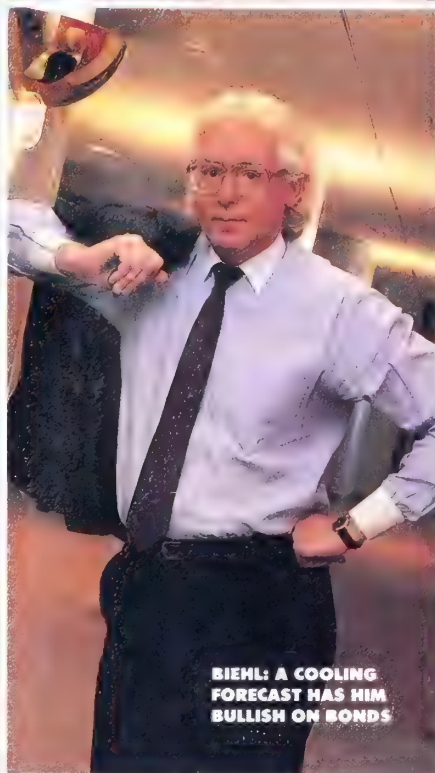
Managing partner Larry Biehl is now urging clients to cut their stakes in stocks to 15% of assets. That's the lowest stock exposure Bailard has ever recommended, down sharply from 23% during the first quarter.

Biehl says equity holdings should be limited to defensive stocks that will do well in the very slow-growth economy—or recession—that his firm sees ahead. When the economy cools and interest rates drop, insurers can take gains on their huge bond portfolios (Bailard urges clients to put 35% of their money in domestic bonds).

Not just any insurance stock will do. Biehl prefers those he sees as potential takeover targets, too. Among them: American International Group (AIG), a large insurance holding company trading at 78, which Biehl figures is worth more than 100 based on its historical price-earnings multiple; Beneficial, a consumer-finance and credit-insurance company selling for 48, but whose assets are believed to be worth \$75 a share; and insurance broker Marsh & McLennan, currently trading at 62, which Biehl estimates is worth 85.

OLD HAND. AIG's earnings have grown at an annual rate of 20% since 1972, outscoring the 16.8% average of other growth stocks and the Standard & Poor's 500-stock index's 9.2% rate. Because it's an old hand at global business, with 50% of earnings coming from overseas, AIG should benefit from the opening of the European Community in 1992. Even at a price well above its \$13 billion market value, the company is tempting to well-heeled foreign insurers.

Beneficial, on the other hand, has tremendous domestic assets and a clean balance sheet. The company opened its books to 20 potential suitors after it rejected a hostile bid in 1988 from Allegheny Corp. Says Art Micheletti, director of portfolio strategy at



BIEHL: A COOLING FORECAST HAS HIM BULLISH ON BONDS

Bailard: "It's just a matter of time for a buyout to occur."

Marsh & McLennan has been buying its own shares, and there are whispers that several Japanese companies want to break into the U.S. insurance business. Micheletti says Marsh's efficient distribution network, vast business contacts, and good customer ties make it "an ideal target for the Japanese."

EYES ARE ON A PLASTICS PRIZE

When a New York arbitrageur tipped a client in January that Aristech Chemical was a super takeover candidate, the idea seemed far-fetched. No rumors were swirling then, though the stock had crept up to 30 from 25 in mid-December. But by late February, Salt Lake City investor Jon Huntsman announced that he was seeking Federal Trade Commission clearance to buy up to 15% of the company's shares. The next day the stock vaulted from 31 to 38. Since then Aristech shares have eased to 34 in quiet trading. But don't be fooled.

Huntsman, chairman and CEO of Huntsman Chemical, which is 40% owned by Great Lakes Chemical, may not be the only party eyeing Aristech. This major producer of polymers and related plastic products is being scruti-

nized by several European and Japanese chemical giants, says one takeover adviser. Management owns almost no shares, so Aristech is "a prime takeover target" for any of them.

Aristech is trading at just 4.4 times 1989 estimated operating cash flow of \$8.35 a share, or 5.4 times estimated earnings of \$6.25 a share. One analyst believes that earnings will skyrocket next year, to \$11, as chemical prices continue to rise and Aristech continues to buy back shares. He says that makes Aristech worth at least \$58 a share based on a conservative price of

High cash flow has enabled Aristech to repurchase 5 million shares since 1987. With hardly any debt, the company plans to buy back an additional million of the 23.6 million shares outstanding. And management may do a leveraged buyout or a recapitalization to avoid a takeover, says the analyst.

Aristech has already borrowed to buy more shares for its employee stock-ownership plan and has put other antitakeover measures in place. But says one pro, if a rich offer materializes, it will be hard to resist.

NOTHING ROUGH ABOUT THIS DIAMOND

With crude-oil prices on the rise, it isn't hard to understand why shares of Diamond Shamrock Refining & Marketing have risen from around 15 in January to nearly 22. Diamond is one of the purest plays in oil refining. And as a gasoline retailer, it stands to gain handsomely in the summer, when seasonal demand boosts prices.

But some big investors have been snapping up shares because they see Diamond as an undervalued asset play. The company, spun off in 1987 by Diamond Shamrock (now Maxus Energy), sells gasoline and diesel fuel in eight states through about 2,000 gasoline convenience store outlets. Says Bill Harnisch, president of Forstmann-Lauden Associates, which has accumulated a 17% stake: "Diamond's assets are worth about \$35 a share based on the prices fetched by other independent refiners in recent deals like Pacific Petroleum."

Harnisch has upped his earnings estimate for the year, and he thinks other big asset players will start buying soon. Management has been repurchasing stock and, together with the company's ESOP, now owns more than 50%

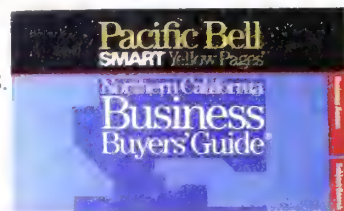


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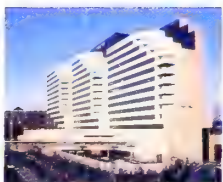
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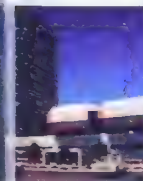
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And Shows.



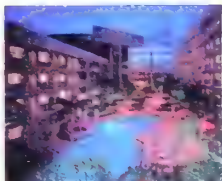
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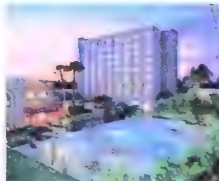
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Photograph courtesy: Bod

Peter Drucker says, "The Salvation Army probably does a better job with the poor than anyone else."

"And frugally," adds *Fortune* (11/9/87). "Of each dollar it receives, 86 cents goes to the needy." In a business where 50 to 60 cents is the norm.

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Economies of scale: We buy like an army. Uniforms wear like

iron and save on pinstripes and power ties. Utilitarian furniture *must* last 10 (upholstered) to 15 (unupholstered) years.

Cost control: We use both sides of all paper and make pads out of the leftovers. Equipment is kept in top shape to last longer. Cost-cutting ideas are encouraged and communicated.

Hard choices: Buying computers and consolidating our four territories might save labor. But cost money. So we keep laboring.

Yet aren't we a religious

group?

Religious, yes. Fanatics, no. Being holier-than-thou doesn't get the job done.

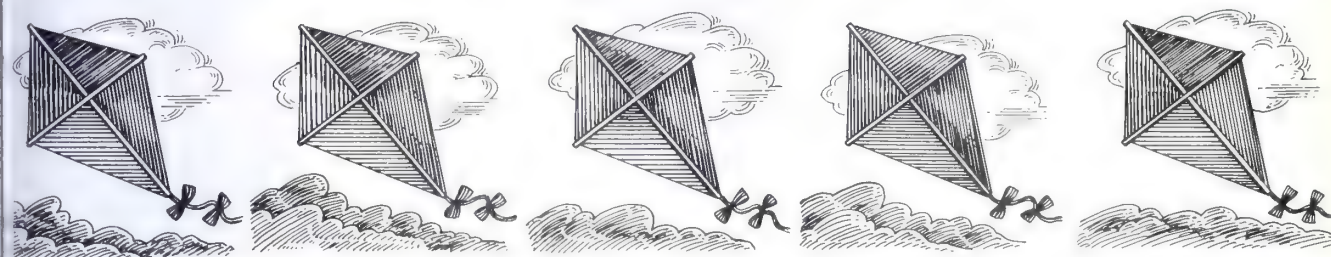
Still, it takes more than just hope and charity to succeed. It takes an act of faith to fight alcohol, drugs, poverty and hopelessness on its own turf—and win.

But we manage it. As Peter Drucker says, "Their achievement is to turn outcasts into citizens."

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The light bulb campaign is already a brilliant success.

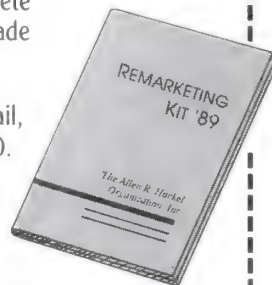


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AMERICA'S INCOME GAP: THE CLOSER YOU LOOK, THE WORSE IT GETS

While the richest keep growing even richer, 20% of U.S. children are growing up in poverty

For most of the 1980s politicians and economists have argued about whether the rich got richer and the poor got poorer under Ronald Reagan. But recent studies indicate that there's not much question left: The U.S. indeed is undergoing a long-term increase in income inequality.

The new evidence stems from a fresh approach some economists are taking. Instead of using the traditional method of studying income distribution among all workers, they're examining income within subgroups of the population, such as married couples with children, or 25-to-34-year-olds, or Hispanics. This avenue has only just begun to be explored. The Congressional Budget Office (CBO) took one of the first looks in early 1988. Then, in December, the Census Bureau issued a detailed report on subgroup inequalities, using data just for 1986.

DRAMATIC SHIFT. Even so, the first indications already are clear: The gap between rich and poor has widened since 1979, significantly and sometimes dramatically, within most groups (charts). "If you look at subgroups you can see that inequality is rising more than it seems to be if you just look at the aggregate numbers," says Sheldon Danziger, a sociologist at the University of Michigan. "There's a lot more going on in the pieces than in the larger picture."

The implications are fairly somber. For one thing, poverty may have become more intractable. In the 1980s the elderly, who previously made up a disproportionate share of the poor, have been replaced by younger adults, who have young children. And children brought up in poverty are more likely to remain poor as adults. "You may be permanently damaged economically by being raised in poverty," says Frank Levy, the author of *Dollars and Dreams: The Changing American Income Distribution*. "The issue is not just inequality: It's the future labor force."

Of course, inequality is not necessarily produced by forces of evil. For instance, one reason that the overall chasm between rich and poor has widened is the baby boom. As that bulge of younger people moved into the work force, the

median age of the average breadwinner fell. Since younger workers tend to earn less than older ones, overall inequality rose. It's not necessarily wrong for individuals to earn more as they gain experience. "We think that these aspects of the world are natural, even though you can't see them at work in the overall measurements of inequality," says Marvin H. Kosters, an economist at the American Enterprise Institute.

Such factors are part of the reason that the traditional methods of analyzing income distribution haven't produced a clear verdict on inequality. One typical

growth rates of the top and the bottom was 13.4% greater in 1987 than in 1979.

When you divide the population into subgroups, the picture gets even worse. The CBO found growth-rate spreads larger than 13.4% in all of the groups studied. For example, the income growth gap for single mothers has shot up since 1979. Why? In part because women who have made their way into the professions and small-business ownership. Most women used to be confined to occupations that pay less than those open to men. As a result, unmarried, divorced women from middle-class fam-

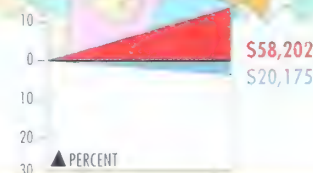
RICH VS. POOR: THE GAP WIDENS

PERCENT CHANGE IN
HOUSEHOLD INCOME
FROM 1979 TO 1987*

■ LOWEST EARNER IN TOP 20%
■ HIGHEST EARNER IN BOTTOM 20%
1987 INCOME LEVELS ARE SHOWN

MARRIED COUPLES
WITH CHILDREN

SINGLE MOTHERS
WITH CHILDREN



*FIGURES ARE ANNUAL IN 1987 DOLLARS, AND ARE ADJUSTED FOR AVERAGE FAMILY SIZE

approach economists have used is to divide the population into five groups: the highest-paid 20% of all families, the next highest-paid 20%, and so on. Then they compare how each quintile has fared. The CBO did this for the income of the top and bottom 20%. After adjusting for inflation, it found that the average income of a family that was representative of the poorest 20% fell by 1.4% between 1979 and 1987. They have less purchasing power today than eight years ago. Meanwhile, a typical family in the top 20% has done rather nicely: their real earnings rose 12%. Put another way, the spread between the income

families earned little more than women from working-class backgrounds.

But in recent years, some educated women—usually from better-off families—have made strides in higher-paying fields such as medicine. Others have become small-time entrepreneurs. As a result, differences have begun to develop among women workers, pushing up the income bracket of the top 20% of single mothers. "Rising divorce rates may have expanded the number of middle-class single mothers, making the group more diverse and causing a rise in inequality," says Kosters.

Leslie Johnson is a good example. In

ed a florist's shop in Hightstown, in 1975 and earned \$25,000 to 30 a year. In 1984, she sold the shop and moved to St. Paul, Minn. She now runs another flower store running just as well as her first. Johnson recently opened a second shop and says she now takes home more than \$40,000 a year—which puts her slightly ahead of inflation since the late 70s. "It's been difficult raising my son myself," says Johnson. "But now the balance is doing well."

BEHIND. By contrast, single mothers at the bottom are being left behind. Women who have no jobs, such as mothers on welfare, have not benefited from the economic recovery—either through job payment or wage gains. "Also, some benefits have been cut or not raised in inflation, which worsens the position of mothers on the bottom," says David Elwood, a sociologist at Harvard University.

Resa L. Matos knows what he means. The single mother of three has spent most of the past 12 years on welfare. In 1977, Matos had one child and was paid \$400 a month. Today, with two children, the San Diego resident

gave a proportionately bigger income boost to the truck driver," says Heidi I. Hartmann, head of the Institute for Women's Policy Research in Washington. That's less true today: A doctor's wife might be a doctor herself. "Women's work no longer equalizes family income as much," says Hartman.

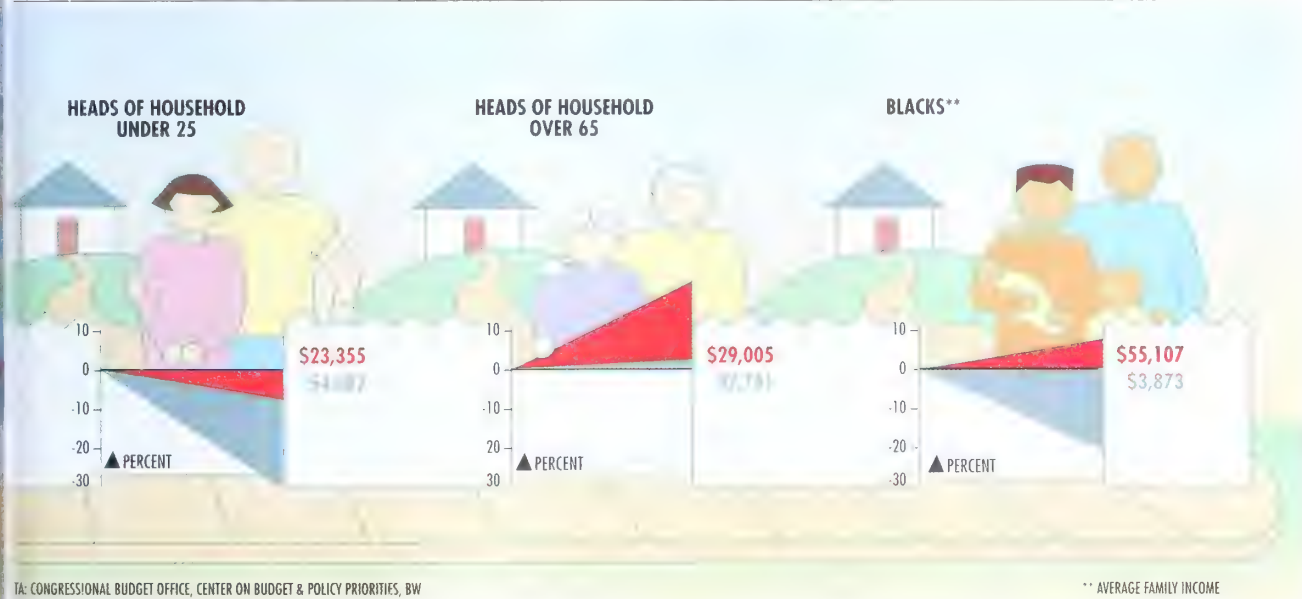
One of the greatest disparities of the 1980s has been among blacks. The spread between the income-growth rates of the bottom and top families has shot up 29% since 1979, more than for any other group studied so far. This is consistent with the rise of a black middle class. Unfortunately, it doesn't mean that many blacks have overcome discrimination and moved into higher-paying jobs. Indeed, only 5% of the net new jobs gained by blacks since 1979 paid \$18 an hour or more, compared with 18% of new white jobs, according to Bennett Harrison, an economist at Massachusetts Institute of Technology. "What's happening is that two black earners have lousy jobs, but they are packaging them together to get one middle-class family income," says Harrison.

The new perspective on inequality helps to illuminate differences among

Young people have been the big losers. The real average income of families headed by people under 30 has plunged 14% since 1973, according to the Children's Defense Fund. Demographic trends, such as the increase in single mothers, have played a part. But the chief culprit seems to be the slow growth of wages since 1973. Young workers have been hit hardest because they joined the job market most recently: the last-hired, first-fired syndrome.

The outcome has been a divergence of income growth for young and old—even excluding the elderly. Fifteen years ago families headed by people under 30 earned 38% less than families headed by 30-to-64-year-olds. Today young workers earn 58% less. "Young workers have been hit the hardest and show no sign of recovery," says Robertson C. Williams, author of the CBO report.

POOR KIDS. The greatest victims are children. The poverty rate of the under-30 crowd has nearly doubled since 1973, to 22%. This increase, along with such factors as the tendency of wealthier couples to put off starting a family and the rise in single mothers, has put 20% of children in poverty, up from 14% in 1973.



\$790 a month; if she still had one child, the grant would total only \$500. When I started, my rent was \$225 a month," says Matos, who recently landed a job as a clerk. "Now it's \$780 a month. I haven't kept up with inflation." The growing economic changes and the growing economic changes among women also have increased income inequalities among two-earner families. "In the past, if the doctor's wife and the truck driver's wife went to work, they both earned the same, which

gave a proportionately bigger income boost to the truck driver," says Heidi I. Hartmann, head of the Institute for Women's Policy Research in Washington. That's less true today: A doctor's wife might be a doctor herself. "Women's work no longer equalizes family income as much," says Hartman. One of the greatest disparities of the 1980s has been among blacks. The spread between the income-growth rates of the bottom and top families has shot up 29% since 1979, more than for any other group studied so far. This is consistent with the rise of a black middle class. Unfortunately, it doesn't mean that many blacks have overcome discrimination and moved into higher-paying jobs. Indeed, only 5% of the net new jobs gained by blacks since 1979 paid \$18 an hour or more, compared with 18% of new white jobs, according to Bennett Harrison, an economist at Massachusetts Institute of Technology. "What's happening is that two black earners have lousy jobs, but they are packaging them together to get one middle-class family income," says Harrison. The new perspective on inequality helps to illuminate differences among

Over the long term, this may be the worst effect of rising income inequality. Many researchers have found that poverty tends to perpetuate itself. "For instance, 36% of girls from welfare families end up on welfare as adults, while only 9% of those from nonwelfare families do," says Sara S. McLanahan, a sociologist at the University of Wisconsin. In the not-too-distant past, being born poor usually meant dying poor almost everywhere in the world but in the U.S. The thought that this may happen here is troublesome in a country which claims to take equality of opportunity seriously.

By Aaron Bernstein in New York

Hyundai has conquered

Introducing the new Sonata from Hyundai. It has more passenger room than any other car in its class. And the power to fly.

These days a lot of mid-size cars promise you the moon. But check their interiors first to see if there's any space that goes with them. Usually there's not much.

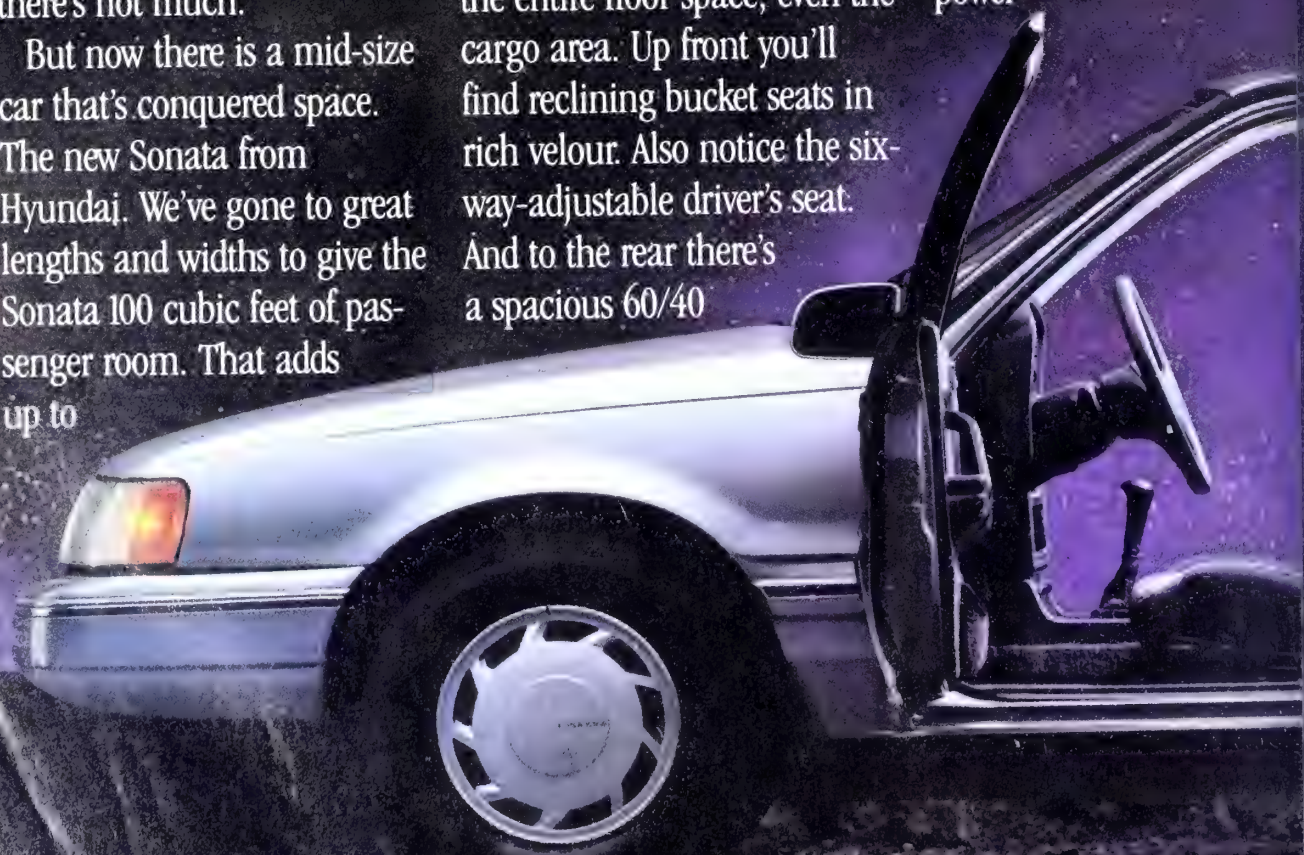
But now there is a mid-size car that's conquered space. The new Sonata from Hyundai. We've gone to great lengths and widths to give the Sonata 100 cubic feet of passenger room. That adds up to

more room than any other car in its class. It also adds up to a very comfortable ride for five adults. Including their elbows and shins.

As a matter of fact, inside the Sonata GLS you'll discover room for everything but improvement. There's an ergonomically designed dash with full instrumentation that helps eliminate the awkward reach. Plush cut-pile carpeting covers the entire floor space, even the cargo area. Up front you'll find reclining bucket seats in rich velour. Also notice the six-way-adjustable driver's seat. And to the rear there's a spacious 60/40

split bench seat that folds to make a large cargo area larger. The rear seat even has a disappearing center arm with added storage space.

The Sonata GLS also comes equipped with a whole gamut of standard features. Features that will put you in complete power. Like power windows and power



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AARON SPELLING 'ILL IN HIS PRIME TIME?

TV mogul is dealmaking frantically to get back on top



Aaron Spelling was Hollywood's exemplar of TV success during the 1970s and early 1980s. A one-time struggling actor, Spelling became one of the small screen's best-known producers with such smashes as *Charlie's Angels*, *Dynasty*, and *The Love Boat*. Their popularity helped him amass a \$200 million fortune and build a 56,000-square-foot Beverly Hills mansion complete with an ice-skating rink. But Spelling's hot streak cooled five years ago—he has produced seven flops since then. Earnings at Aaron Spelling Productions Inc., the company he took public in 1986, have been steadily declining.

Now critics are saying that the 65-year-old Spelling has lost his golden touch. His *Life with Lucy*, starring Lucille Ball, lasted only eight weeks in 1986. To add to his woes, his promising new show, *Nightingales*, is being called demeaning to women.

ON THE CHEAP. On Mar. 1, in an attempt to revitalize his company, Spelling merged his production company with Worldvision Enterprises Inc., which distributes syndicated TV shows, and Laurel Entertainment Inc., a small producer of low-budget movies and syndicated hor-

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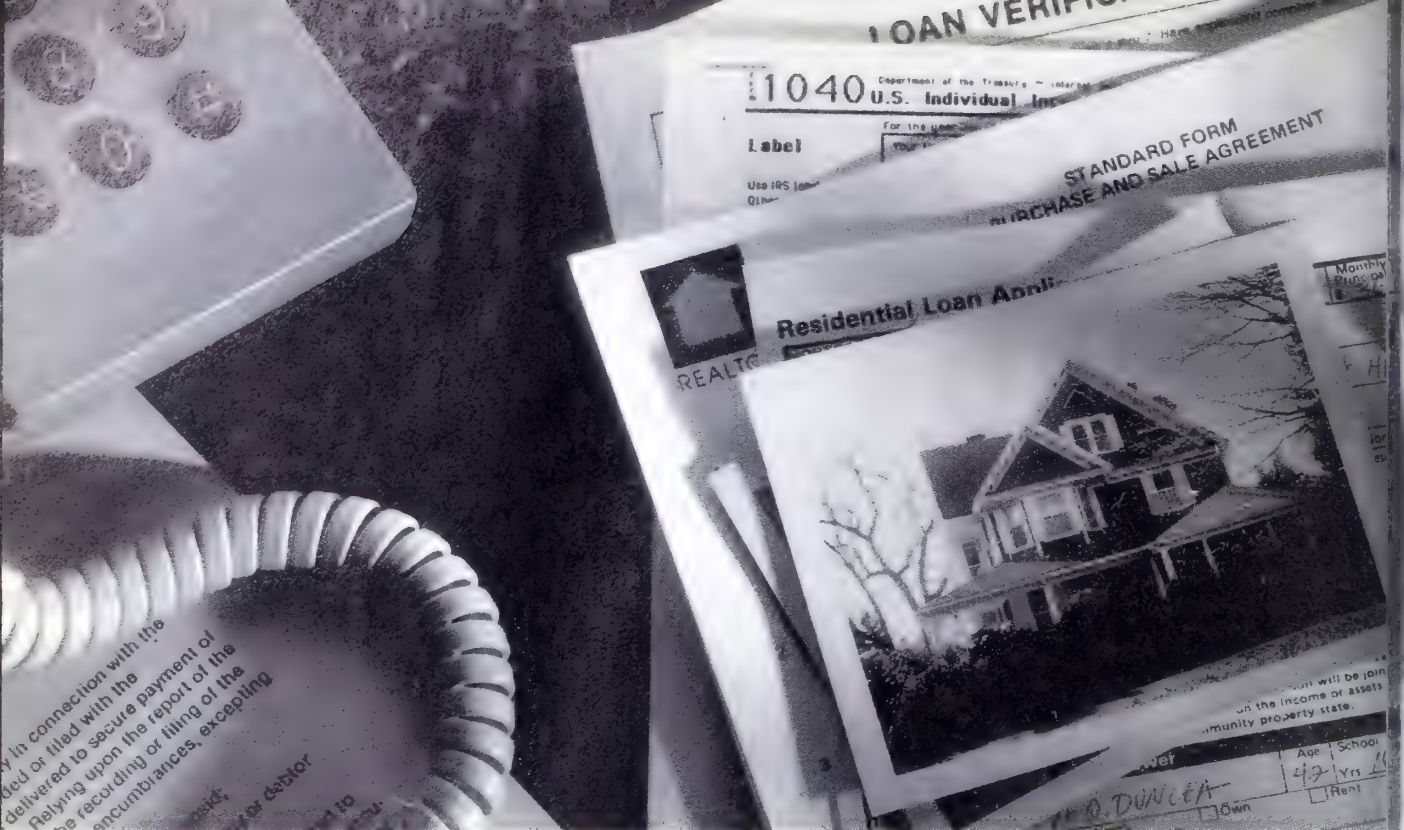
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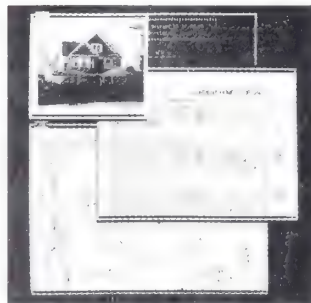
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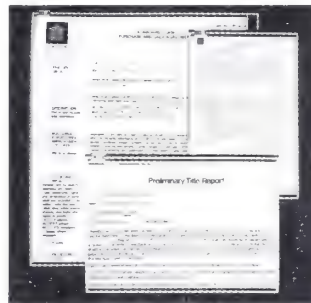
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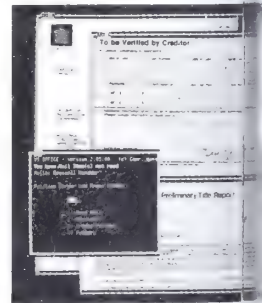
*Customer comes in for a mortgage.
Has a loan application, tax returns.*



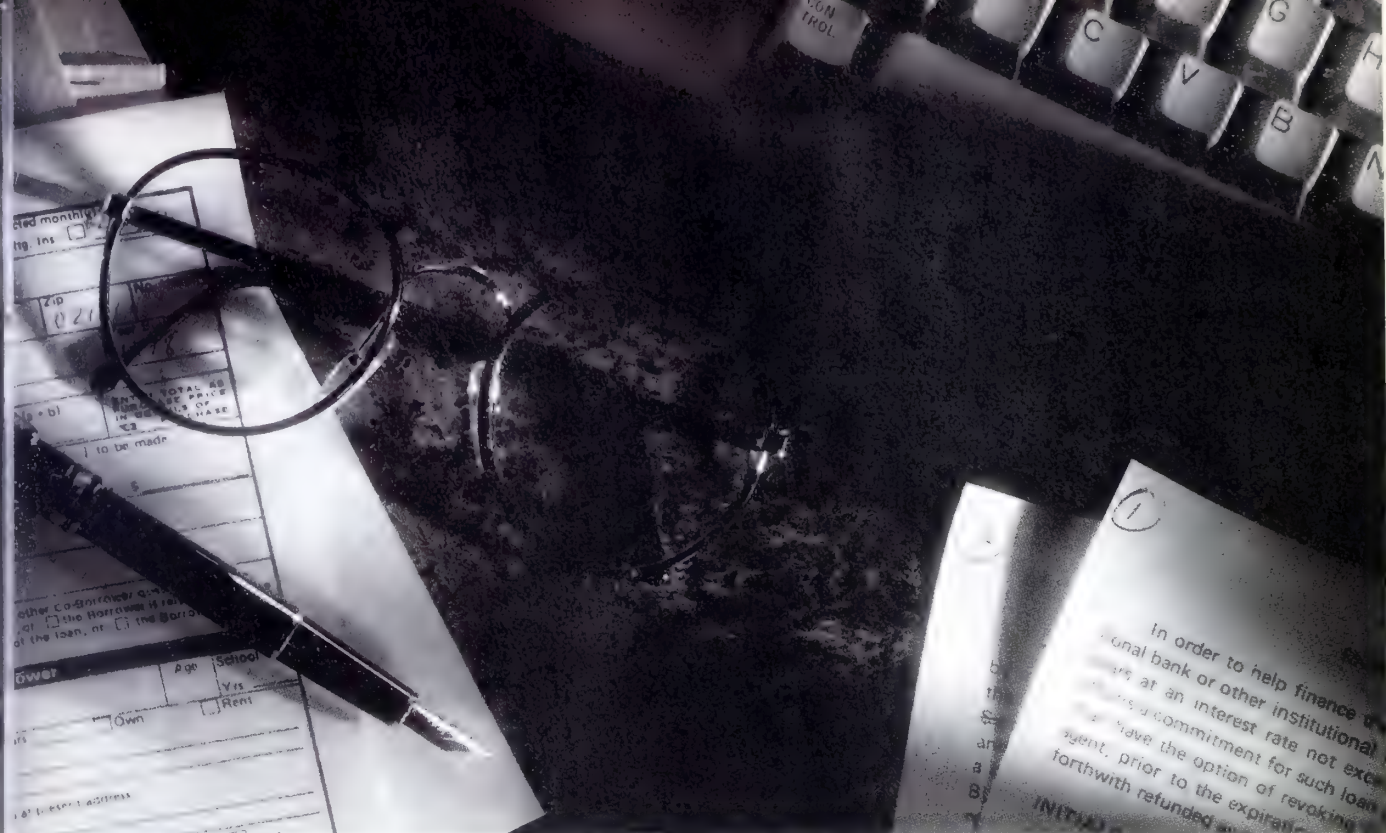
*Bank appraiser mails in photos of
property, plot plan and comparables.*



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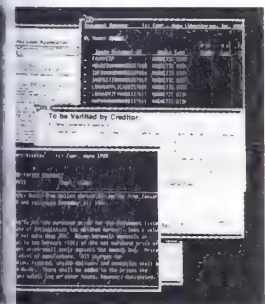
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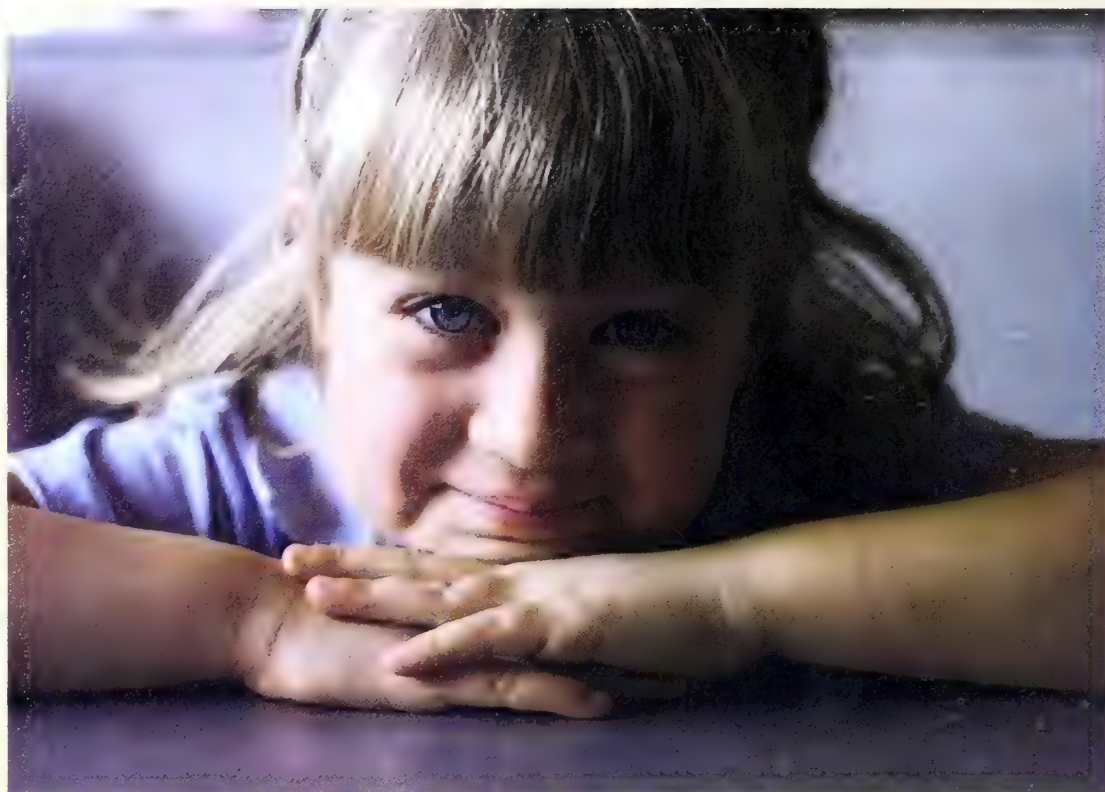


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BusinessWeek



programs such as *Monsters* and *from the Darkside*. Meanwhile, Spelling is churning out TV pilots—five of which the networks are considering for fall.

Spelling's \$120 million company has debt and can easily afford Worldvision and Laurel. Spelling paid Carl H.

er's Great American Communications Co.

million for

division and gave

Cincinnati financier

al of 49% of the

created company,

called Spelling Entertainment Inc. In addition,

he paid \$9 million in

and stock to buy

l. Spelling is chair-

of the new firm and

2% of its stock.

Spelling got the com-

pany cheap—but neither one is a prize.

Worldvision hasn't bought many new

shows lately, and its earnings are flat.

Spelling lost money in the most recent 18

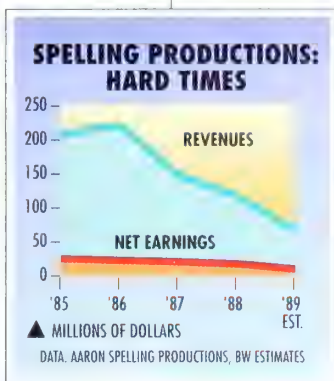
months for which numbers are available.

Spelling is betting that his merged

companies can resolve some of the prob-

lems that each faced on its own. He and

Laurel needed to reach new markets, and Worldvision needed more shows to distribute. Spelling also expects Lindner to lend a hand. Great American's Hanna-Barbera unit, creators of such cartoons as *The Flintstones*, may jointly produce shows with Spelling that Worldvision can distribute.



FEW TAKERS. The new shows will help: Spelling's older programs have run their course. Domestic sales peaked in 1986. Warner Brothers Inc. distribution can't find enough takers for *Hotel*, a successful prime time soap. Smaller markets overseas may provide additional sales for the older shows.

Spelling blames ABC Inc. for the failure of

Lucy and his other newer shows. He maintains that the trouble started after Capital Cities Communications Inc. bought ABC-TV in 1986. "They began turning down my pilots and giving my shows lousy time periods," he says. That was a big blow: A contract dating from 1969 gave ABC exclusive rights to Spell-

ing productions until 1987. ABC executives declined to discuss Spelling.

Now a free man, the producer has found other networks more receptive. NBC demonstrated its faith last year by picking up *Nightingales*, a drama about nurses. The show healed NBC's Wednesday night ratings—but attracted unwelcome controversy. Two major advertisers, Sears, Roebuck & Co. and Chrysler Corp., pulled out when nurses' groups objected to the characters who seemed more interested in sex than medicine. Spelling is defensive about the charge. "I am not a T-and-A producer," he says, pointing to more highly regarded shows such as *Family*.

The reviews from Wall Street can hardly be called raves. Spelling's shares, which went public at 14, currently trade at about 7½. They rose nearly a point after the company completed its recent mergers.

While Spelling no doubt would love to see his stock price improve, he isn't complaining too loudly. As he sits in a mammoth, wood-paneled Hollywood office, he savors his past successes. *Nightingales* looks like his first winner in a long time. But he still needs more.

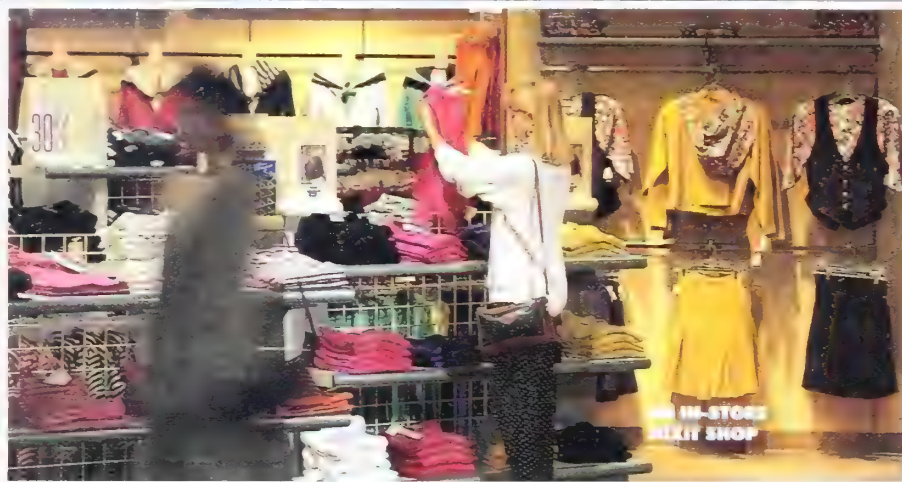
By Ronald Grover in Los Angeles



With the way some facsimiles make you wait,

THE NEWLY MINTED PENNEY: WHERE FASHION RULES

The chain finally sees results from a painful makeover



When J. C. Penney Co. flipped on the switch to its Telaction network in 1987, it heralded the service as a quick and easy way to shop using two home staples: a TV and a push button phone. Selected cable subscribers in Chicago would dial an access code, navigate a sea of retail offerings on their TV screens, and order goods by phone. Penney officials saw such interactive home shopping as the wave of the future. But the wave never crested. Mar. 30, after sinking \$106 million in the venture, Penney pulled the plug on Telaction and said it would take a million earnings hit in the first quarter.

The shutdown caps a disruptive year for Penney, which has been struggling for much of the 1980s to recast itself from a dowdy general merchandiser to a moderately priced fashion specialist. That makeover has handed the 1,355-store department-store chain some early results. Last year income before recurring items fell 5.4%, to \$668 million on a 3% sales decline, to \$15.3 billion.

Yet retail experts see a stronger Penney emerging from behind those disappointing numbers. They praise Penney for its willingness to experiment



you'd think that you had nothing better to do with

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ent formats—even if some, like tion, ultimately flop. They say the handise and store displays look bet- han ever, and catalog sales are shing, with sales growth of 13.7% 88, to \$2.9 billion. February sales up 7% on continuing lines in stores more than a year, and analysts ex- Penney's overall sales to show 4% gains in 1989—pro- the economy holds ays Clark A. Johnson, man of Pier 1 Imports "They're doing a ter- job of repositioning, 's been a long, ardu- process."

TECH. As part of that itioning, the company sting some new spe- concepts, including a store-within-a- featuring coordinated el for young women, Portfolio, an upscale ure outlet. And Penney is not loning home shopping completely. tion didn't work because the inter- technology turned out to be much expensive to develop than Penney ted. And subscribers were mostly g groceries, not higher-margin ; that would make the investment

worthwhile. So Penney is going for a straight home-shopping TV program. In March it took control of the Shop Televi- sion Network Ltd. and will begin selling merchandise from its catalog on the channel this month.

Penney's efforts to remake itself came to a head last year when it moved its headquarters to the Dallas area, leaving

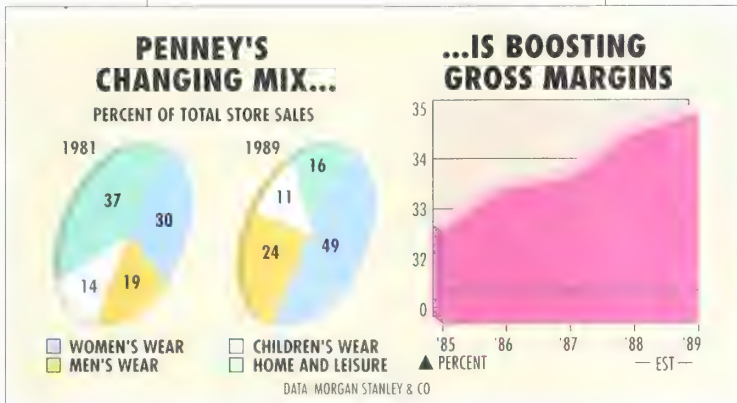
in many stores. That contributed to a 3.6% drop in December sales at stores open more than a year.

Despite such hitches, Penney's strate- gy is bearing fruit. Thanks to the elimi- nation of three unprofitable hardgoods lines—home electronics, sporting goods, and photography—gross margins have climbed steadily upward (charts). Even the Christmas shortage helped margins: Stores had less to mark down after the holidays.

With the hard part of the move behind it, Penney is now concentrating on its retailing projects. Being in Texas helps. In their mid- town Manhattan perch, Penney executives were isolated from the chain's middle-market, heartland audience. They had to drive at least a half-hour to visit the closest store.

Now the nearest one is across the street, so managers can mingle with customers and keep tabs on new merchandising displays.

The area they watch most closely is apparel. Penney merchants have essen- tially given up on an earlier strategy of marketing exclusive designer names



behind 2,100 of its 3,300 New York em- ployees. The relocation should save more than \$60 million a year—but it has been painful. Especially hard hit was the buy- ing staff, which lost many seasoned vet- erans. Their inexperienced replacements failed to order enough merchandise for the Christmas season, causing shortages

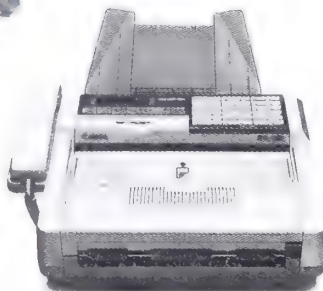


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such as Halston and Mary McFadden to the masses. Instead, they're improving their private-label fashions and adding more national brands, such as Levi's and Bugle Boy.

JUNIOR MISS. Mixit, Penney's answer to such successful retailers as The Limited, shows where the company is heading. Started a year ago with 105 shops in regular Penney stores and one free-standing unit, Mixit sells contemporary mix-and-match clothes and accessories. The division initially focused on young juniors, but officials say sales did not meet expectations. They have since aimed the merchandise at older customers, and sales have improved. The company is deciding whether to roll out Mixit as a separate chain.

Penney is developing other specialty projects, too. Units, acquired in December, 1987, has opened 143 stores selling

one-size-fits-all knit separates and is expanding into Great Britain, Canada, and Mexico. Next fall Penney plans to launch Amanda Fielding, a women's apparel chain. The three Portfolio furniture stores, which sell knockoffs of Ralph Lauren and other designers, are averaging \$300 a square foot in annual sales, more than double a Penney store rate. Eight more will open this year. "With the changing expectations of customers, we must try lots of different formats," says Terry S. Prindiville, executive vice-president.

Even if some of these concepts don't work, they should provide merchandising insights that will help the Penney stores. As Penney has learned, move two steps forward and one step back is better than standing still.

By Amy Dunkin in Dallas, with Brian Bremner in Chicago

PENNEY ISN'T THE ONLY CASUALTY IN HIGH-TECH HOME SHOPPING

With J. C. Penney Co.'s hasty retreat from interactive home shopping, it's time to put up another tombstone in the crowded graveyard of high-tech retailing. Penney is in good company: Knight-Ridder Inc. and Times Mirror Co. also lost millions on failed ventures that let people shop, bank, and receive data at home. But this latest failure to sell two-way services beamed to homes by TV or computer suggests that retailers are pursuing an idea whose time has not come.

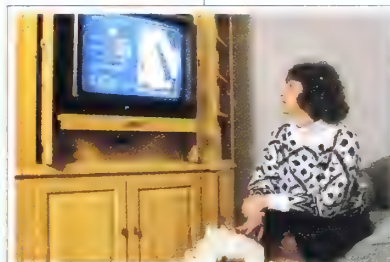
Penney's debacle, which cost \$106 million, came because its Telaction system was not ideal for electronic home shopping. Telaction, which connected about 30 retailers, required subscribers to use time-consuming commands to wade through various menus. Telaction's "party line" design, with 15 families sharing a loop, often left viewers waiting until a neighbor finished shopping.

MALL POX? Telaction's misstep raises doubts about how many consumers prefer to shop electronically rather than at malls. Yet some retailers still see a bright future for low-tech varieties of home shopping. Last year consumers spent about \$1.4 billion through TV programs that allowed

them to order by telephone, and industry sales should grow 20% in 1989.

Even that business has seen a shakeout, though. Since 1986 some 25 home shopping programmers have gone under or been gobbled up by competitors, according to Paul Kagan Associates Inc. Now the business is dominated by three players: the Home Shopping, Cable Value, and QVC networks. Penney recently acquired the smaller Shop Television Network.

The shutdown of Telaction leaves the interactive home shopping business with a few systems. Sears and IBM continue to roll out their Prodigy network, formerly called Triniton, a PC-driven system. But they don't expect a profit for several years. GTE is testing a service



TELACTION: AHEAD OF ITS TIME?

Boston, and Southwestern Bell has unveiled a trial network in Houston.

But the glory days for such ambitious networks will probably arrive only after the home computer becomes a bigger part of life. Laments Howard E. Wall, president of Post-Newsweek Cable Inc. and a booster of interactive services: "The generation in power isn't used to computers, and we don't tend to use them." For now, shopping mall owners have little to fear.

By Brian Bremner in Chicago

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ESTIMATE

Client: Scott Tuthill
Address: 675 Deer Park Road
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State: ID Zip: 83703

Project: West Wing Addition
Project No: MC66224-89
Client Phone: 619-555-2887

Description	Materials	Labor	Total
Hardware	1,709	0	1,709
Painting	1,440	9,000	10,440
Concrete	15,000	9,000	24,000
Plumbing	3,250	3,000	6,250
Carpet	1,500	895	2,395
Lumber	11,000	0	11,000
Framing	0	7,250	7,250
Electrical	811	1,000	1,811
Supervision	0	2,600	2,600
Clean Up	0	0	0
Permits	898	2,344	3,242
Total			71,097

Comments: The estimate above is based on constructing the West Wing according to the plans and working drawings submitted for Scott Tuthill by Jarl Johanssen and Associates, architects. The construction would be completed within 6 months of breaking ground.

Signature: _____

Vendor: Pine Tree
Address: 12311 Indi
City: Boise
State: ID

Lumber:
2x4x
4x4x
2x4x
4x4x
2x4x

Total
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INFORMATION MANAGEMENT

FUTURE SHOCK IS RATTLING THE FUTURES PITS

Chicago traders are spooked by the specter of automation

may be archaic, but that's Chicago for you. Standing cheek to haunch in an octagon-shaped pit, traders shout and flash hand signals as they haggle the prices of futures in currency, culture, and other commodities. To the dismay of its practitioners, the madhouse, open-outcry system may soon be out to change. Both the Chicago Board of Trade and the Chicago Mercantile Exchange—the world's dominant exchanges in futures—are about to try computerized trading on an after-hours basis.

And that's fanning the type of man-machine dispute that has characterized many major automation projects. The exchanges have promised not to computerize trading during day-hours. But lots of brokers think that's temporary—and that 150 years of tradition is in jeopardy, along with some of their jobs. "The floor brokers will be the first to go," says one Chicago trader. They plan to match up orders on a computer, there's no reason to have shouting orders in the pits."

Naggers at the exchanges play down disruptions. To them, computerization will help restore confidence in the exchanges, which have been rocked by recent charges of cheating customers. It's the key to cashing in on the rapidly growing international futures business. Says Leo Melamed, chairman

of the Merc's executive committee: "Technology is dictating the future."

Indeed, the future is here. Exchanges in Tokyo, London, and Zurich—currently automated or about to be—are stealing business from Chicago. They're cutting especially into the global market for financial instruments such as interest-rate and foreign currency futures. While the CBOT's volume nearly doubled in the past four years, its global market share fell four points, to 33%.

To counteract this, the Merc and the CBOT both are developing automatic trading systems, called Globex and Aurora, respectively. Each hopes to persuade other exchanges to use its system for selling Chicago futures products and for brokering their own instruments through Chicago's traders. This will provide international customers 24-hour access to Chicago and give the exchanges up to \$40 million in new annual revenues. Last month, in Boca Raton, Fla., the ex-

changes blitzed two dozen overseas trading executives with slide shows highlighting the systems. It's not clear if anyone was impressed. "We have yet to make a choice," says Michael Jenkins, who heads the London International Financial Futures Exchange (LIFFE).

MIGHTY MOUSE. So far the Merc, which has been working on Globex for more than two years, is ahead of the CBOT, which won't finish Aurora until 1990. The Merc already has persuaded three other exchanges to join Globex when it starts up later this year: the New York Mercantile Exchange, the Sydney Futures Exchange, and the Marché à Terme International de France (MATIF).

Globex is the system traders fear most. With it, they enter anonymous buy and sell orders, which are automatically matched according to price and time. There's no haggling between traders.

Aurora, by contrast, is a computerized version of the current system. With it, traders call a particular futures instrument up on a screen. As trades are entered, buyers and sellers and the time and price of their bids are identified by color-coded icons. A trader uses a "mouse" to move the buyer's icon onto the seller's. He presses a button to execute the order. Unlike Globex, which ceases trades instantly, Aurora lets traders interact and make price and bid changes until the trade is completed.

Despite their differences, Globex and

WHERE THE ACTION IS



Information Processing

Aurora are similar in a crucial way: They provide audit trails that can uncover the types of trading abuses allegedly found by the FBI during a recent two-year probe. Among them: cheating customers out of the best prices, altering trading records, and manipulating the markets. Indictments of nearly 100 traders are expected later this year.

LOSING THE FEEL. Traders want more safeguards, but they also want to preserve their livelihoods. Exchange seats can cost as much as \$500,000, and they offer the chance to earn millions. If computers cut that income, the price of seats will fall. And computers won't just automate trading, they'll redefine it. Traders traditionally work by gauging the "feel of the floor": Who's buying what and how much? Who's crowding which pit? Who looks cocky? Who doesn't? "These guys don't play the market," says Larry Hite, managing director of Mint Investment Management Co., a New York-based commodities fund. "They play the other guy. People read each other. And they don't want to learn a new game."

Some traders argue that computers will eliminate this challenge of outwitting each other. If that's true, they say, it could stem the supply of dollars feed-

ing the markets—and impair the liquidity that keeps trading active. Says Joel Jacobson, a veteran CBOT trader: "Locals keep the market fluid."

Managers at the exchanges are caught between the traders, who in essence own the exchanges by virtue of the seats they hold, and customers, who generally favor computerization. Typical of the latter is the National Cattlemen's Assn. It recently weighed in as favoring electronic trading, citing record-keep-

**'If they plan to match up
orders on a computer,
there's no reason to have us
executing orders in the pits'**

ing and market surveillance advantages.

The Merc and CBOT managements promise that Globex and Aurora will remain overnight trading systems. But analysts think they're saying this mainly to placate traders. According to one Chicago futures expert, pro-automation power brokers at the Merc, such as Melamed,

who have increasingly consolidated strength, will ensure that "computers will take over the floor within the next 10 years." The CBOT, he adds, may move more slowly toward computerization because the traders have a greater say in management decisions.

But even that could be wrong. Individual traders may be steamrolled by institutional investors such as Morgan Lynch & Co. and First Chicago Capital Management, which also own exchange seats. Most of these brokerages have broken with the floor traders and are pushing for computerization, which would tie in more with their own automated systems. Jack A. Barbanel, senior vice-president at Gruntal & Co., a stock and futures brokerage firm: "The institutional houses have brought a tremendous amount of business onto the floor and have significant leverage."

Before it's all over, the 6,000 Chicago futures traders most likely will be losers in this battle. Given the pit mentality, however, it may not take long for them to adjust. Which conjures up an entirely new image of Chicago's futures bulls: trader nerds.

By Kathleen A. Behof in Chicago, and Jeffrey Rothfeder in New York



WHO'S PLUGGING IN THE CHICAGO EXCHANGES

four leading high-tech companies—Apple, Digital Equipment, Texas Instruments, and Tandem—are behind Globex and Aurora. They're gaining a foothold in what many feel will be a hot market for the next decade. Around the world, lots of futures and equity exchanges, not to mention brokerages, are preparing to switch from manual trading systems—expensive ones. "Globex and Aurora pale in comparison with some of the broad markets being put together," says Peter Rensinger, a computer analyst at Chicago-based Duff & Phelps Inc. In fact, the new Swiss Options & Financial Futures Exchange in Zurich built a \$40 million system.

That's not an isolated example. Datacube Inc. Research Director Robert Eron recalls doing a study for the Manhattan Bank three years ago on the technology that brokers were using for trading. "At that point there was little interest in talking about automated systems," says Cam-

eron. But "today almost every firm is spinning out high-value requests for proposals." Adds Robert Pedrazzini, a technology consultant with Arthur Andersen & Co. in San Francisco: "Electronic trading could easily represent a \$1 billion-per-year business for computer makers" in the 1990s.

Reuters Holdings PLC is spending

Apple, Digital Equipment, Texas Instruments, and Tandem are getting a foothold in a hot market

upwards of \$30 million to build the Chicago Mercantile Exchange's Globex system. Reuters is borrowing from its \$110 million Instinet Equity Trading System and its Dealing 2000 System for the technology to carry Globex trades. And an upgraded bank of Digi-

tal Equipment Corp. Vax minicomputers will handle trading information at the Merc itself. Reuters, which will take a fee for each Globex transaction, hasn't chosen a maker for the thousands of terminals that will be leased to brokers and traders. The Merc's investment in Globex: about \$2.5 million for research and marketing.

FANCY GRAPHICS. The Chicago Board of Trade's Aurora system will use Apple Computer Inc. Macintoshes for entering trades. Texas Instruments Inc.'s artificial intelligence group will provide software to draw the on-screen graphics and perform the data analysis. And Tandem Computers Inc. machines will process the transactions. The CBOT won't say how much Aurora will cost. But it'll be more than Globex, analysts say, given Aurora's fancy graphics.

As their markets mature, that's the type of development computer makers need: Another industry that's bullish on their machines.

By Kathleen A. Behof in Chicago and Jeffrey Rothfeder in New York

GEORGE PELINSEY/DENE INDIAN MOUNTAIN GUIDE



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"...the blue rivers, the rainbows ever beautiful, and the stillness. And everywhere so many animals, never afraid. Dall's sheep. Caribou. Moose. Wolverine. More and more I'm guiding naturalists to take pictures. We fly in, or go by canoe and walk the high lands ...maybe four, five miles a day. And night. For it's always light here.

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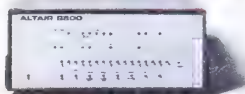
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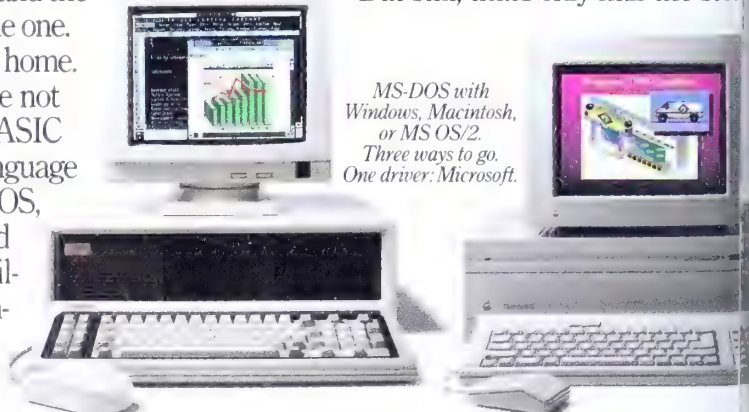
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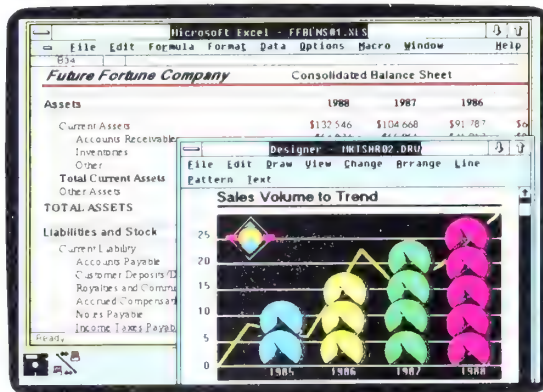
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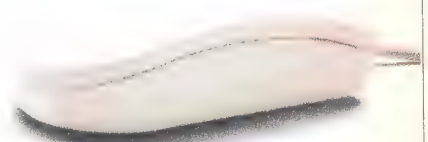
Making it all make sense.

For the first in a series of articles detailing Bill Gates' perspectives on personal computing into the 1990s, call Microsoft at (800) 323-3577, Dept. J33. In Canada, call (416) 673-9811, outside North America, (206) 882-8661.

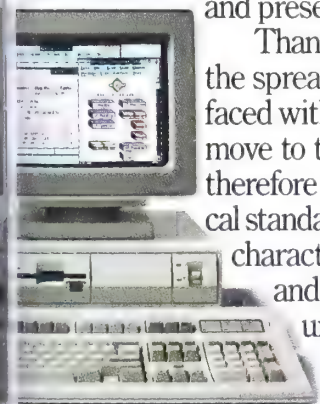
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EDITED BY MARC FRONS

Travel

TAKING A TRIP ON THE WILD SIDE



■ AN IBAN TRIBESMAN OF BORNEO, WHERE VISITORS ONCE WERE BANNED

Work hard, play hard. It's the motto of many an executive. So when it's time to vacation, forget about mere sun and surf: They want adventure. The exotic mainstays—the safaris in Kenya, the treks in the Himalayas, the cruises around the Galapagos—are just the tip of the iceberg. Tour operators are discovering more intriguing locations and innovative ways to take a walk—or a kayak, or a mountain bike—on the wild side.

To experience Africa from a unique perspective, you could take a 27-day safari that covers 4,700 miles—by amphibious aircraft. Mountain Travel's (800 227-2384) Trans-

Africa by Flying Boat trip flies 16 passengers at low altitudes so the scenery below can be seen from bubble-shaped observation windows. The craft, complete with bar and library, lands on remote lakes and rivers, so in 13 stages you can explore parts of seven African countries. The cost: \$13,800, excluding airfare to Zimbabwe.

Mountain Travel's 15-day Borneo Adventure trip (Aug. 10, Dec. 21; \$1,830) offers a closer view of a culture. Ten to 15 travelers hike through rain forests and ply the jungle rivers of this exotic Southeast Asian island. Adventurers observe the daily life of Iban tribesmen. "Until this century," the catalog informs, "Borneo was closed to outsiders and shunned for fear of its cannibal 'wild men.'" Today, the catalog reassures, the Iban "are among the most hospitable hosts in the world."

SADDLING UP. The alien culture you experience may be on the other side of your country, rather than the other side of the world. For Bruce Sherwin, a native New Yorker, adventure meant turning "the whole cowboy myth" into reality by heading out West and saddling up.

In the spring of 1988, Sher-

win flew out to visit the real thing—Two Creek Ranch in Douglas, Wyo.—where he spent five days gathering horses and cattle and driving them over the plains to higher ground. At night, the 17-member crew ate from the chuck wagon and played poker around the campfire before crawling, exhausted, into their tents. While Sherwin admits that he came back "telling everybody that it was like boot camp," he adds that he returned "more relaxed than from any other vacation I've taken." Fall cattle-drive dates are Oct. 21-31 (\$750), or Oct. 21-26 and Oct. 26-31 (\$400).

A good reference for hands-on adventures, both east and west, is Pat Dickerman's *Farm, Ranch & Country Vacations* (\$10.95). It describes more than 200 trips in the U.S. (212 355-6334).

If you venture farther north, to Churchill, Man., you can see its equivalent of the Western plains—the tundra. As the ice in the vast Hudson Bay melts and is blown south, the polar bears hunting seals on the ice migrate inland. There, the 19 travelers on Joseph Van Os Photo Safaris (206 463-5383) observe the bears at close range from "tundra buggies"—chunky four-wheel-drive vehicles with giant tires that raise passengers 12 feet above the ground. That enables you to



■ AFTER SAILING TO SOUTH

pop open the window and start taking pictures without becoming bear food. The week-long polar-bear trip has starting dates in range from Oct. 11 to Oct. 26. Fees are \$1,525 to \$2,075 in Winnipeg, Man.

APPE WATCH. If you're willing to venture into the wilderness, you can come face with another creature that has captured the public attention—the mountain gorilla. Wilderness Travel's (247-6700) Ultimate Primate Safari lets homo sapiens meet some of their closest relatives. In Rwanda, Peter Leberg, a psychotherapist,



■ ROUNDUP TIME: AT A RANCH IN WYOMING, GREENHORNS AND OLD HANDS ALIKE SPEND UP TO 10 DAYS DRIVING CATTLE OVER THE PLAINS



LUXURY LINER, SPECIAL EXPEDITIONS' PASSENGERS VIEW A GLACIER FROM AN INFLATABLE BOAT

e, Ill., along with four travelers and a guide, four different gorilla s over four days, ob- ; them for the pre- hour per day.

ocate the gorillas, your and your trackers set o the forest, hacking growth and following d vegetation or drop- until your tracker finds la family of 15 to 20 rs. When the wild go- gaze at you curiously nere feet away, "you intelligence and real t," says Sternberg. great way to feel one's ss and one's place in rld." The 21-day trip parture dates on June y 19, and Aug. 9. Cost: excluding airfare.

TOUR. If you want a of adventure but like re comforts, many operators offer "soft ure" trips. New York- Special Expeditions (800 3) uses 74- and 80-pas- ships for its many

tours, which include an 11-day voyage exploring southeast Alaska, a good 350 miles away from the disastrous oil spill in Prince William Sound (departures throughout June and August, \$2,400 to \$3,380). Cost excludes airfare. When it's time to explore, passen- gers climb into inflatable mo- tored boats, called Zodiacs, and ferry off.

Other luxury tours are In- ternational Expeditions' (800 633-4734) 12-day cruises on the Amazon River, leaving Jan. 7 and 19. The ship accom- modates about 600 passen- gers. Cruising in comfort is punctuated by visits to underground waterfalls and caves or maybe a ride - on a water buffalo. The cost ranges from \$3,165 for an "inside double" cabin up to \$10,500 for a penthouse cabin with private butler.

For a far more intimate look at South American wil-

derness, there's the 10-room Pousada Caiman Lodge (55- 11-883-6566) located in the Pantanal, the huge wildlife preserve in the western part of Brazil, just south of the Amazon jungle. For your stay of from three to five days, São Paulo executive Roberto Klabin runs "ecological tour- ism," which takes guests by Jeep, horseback, and foot to observe flora and fauna. Room and board runs be-



"TUNDRA SUGGY": A POLAR BEAR GREETSS TOURISTS—WHO HAVE A SAFE VIEW

tween \$135 to \$175 per night.

Another way to immerse yourself in a country is tour- ing by kayak. Sea Trek Ocean Kayaking Center (415 332- 4457) offers trips in British Columbia's Robson Bight Eco- logical Preserve (Aug. 6-12, 20-26; \$775), where brave kay- akers may paddle past killer whales and spot bald eagles. Some other kayaking trips ex- plore Hawaii's Molokai island or Kauai's Na Pali Coast (Mo- lokai: July 1-5, Sept. 2-7; \$1,000. Kauai: June 24-29, July 15-20; \$1,000) and Alaska's Glacier Bay (Aug. 4-10; \$1,100).

'HOTEL BOAT.' To discover more of the variety of such trips, order *Specialty Travel Index* (415 459-4900), a maga- zine that lists more than 150 different activities from hun- dreds of tour operators world- wide. A single issue is \$5.00; an \$8.00 subscription gets you both spring/summer and fall/ winter guides.

If all this is still not quite what you had in mind, there's Abercrombie & Kent's (312 954-2944) Royal Air Tour, a 35-day extravaganza on board a "luxuriously refitted" L- 1011. The \$36,000-per-person program (Oct. 10-Nov. 13) cov- ers half the globe, visiting lo- cales ranging from Bali, Bora- Bora, and Beijing to Nairobi and London. The tour includes gourmet dining, first-class ho- tels, and such special events as an excursion down the Nile in a "hotel boat" and a dinner cruise on Sydney Harbor, complete with a live band. Now that's what we call roughing it. *Suzanne Woolley*

Smart Money

'PAYMENT-IN-KIND' PAPER: WHEN IT'S GOOD...

One nice thing about junk bonds is that their high yield is paid in cash. If the issuer goes sour, you've at least banked some income. You can't say that about the super-junk being dealt out now. It's called "payment in kind," or PIK, paper. Issued as bonds or as preferred stock, a PIK pays interest or dividends in more paper rather than in cash.

PIKs are designed for deals where debt is so large—like the record \$25 billion RJR Nabisco buyout—that the company can't afford to service it all with cash right away.

You may have come in contact with PIKs without really wanting to—as a shareholder in a company that was acquired or taken private. For example, if you

preferred has risen 10% since its issue in late 1988. But many do trade below par, because the market sees "companies carrying an oceanful of debt as susceptible to downturns in the economy," says Natale.

For example, Allied Stores issued 10 million shares of PIK preferred stock on Mar. 10, 1987, with a face value of \$25 a share. The dividend payment is \$3.31 payable in more preferred until 1992, then in cash until 1999. This PIK—it isn't quoted anywhere in the newspapers—is trading at \$10, according to analyst Charles Strausser of Donaldson, Lufkin & Jenrette Securities.

TEMPTING. Based on its depressed price, the yield to maturity in 1992 is an enticing 49.7%. If it endures until 1999, it's 28.4%. Financial pros focus on the earlier year, since PIKs are generally redeemed in full when payments turn into cash or the PIK is first redeemable.

Bottom line: Should the high yields tempt you into buying payment-in-kind paper? If you do, bear in mind that their noncash income is taxable each year. But mainly it depends on your risk tolerance: "Essentially, you're dealing with noninvestment grade paper," says Philip Maffei, a high-yield bond analyst at McCarthy, Crisanti & Maffei. And you could lose it all if the company gets into bankruptcy court. Holders of PIK paper are last in the repayment line, since the securities are junior to everything on the balance sheet but common stock. "When PIKs are good, they are very, very good," says Stephen Albert, a senior vice-president with Kidder Peabody & Co., "but when they're bad, they're horrid."

Stuart Weiss

One pitfall of PIKs: You're in the back of the repayment line

tendered 100 shares of RJR in early February, you'll get \$109 a share in cash for 75 shares. The other 25 shares will turn into PIKs. This is known as a cram-down, as in "cram it down your throat." In a sense, "it's automatically reinvesting in the company," says Robert Natale, an investment officer at Standard & Poor's.

Another way you'll hear about PIKs is from your broker, who might call you to ask: "Are you interested in some paper that could pay up to 50% returns?" Yes, he's for real. But yields that high are usually on PIKs issued a year or two ago by a company that has since suffered a falloff in investor confidence. Not all PIKs drift into discount; Interco's PIK



Autos

THESE CAR WASHES CLEAN EVEN THE INSIDE OF THE GAS CAP

Surveying the grime on your car, you decide it's time for drastic action. No mere car wash this time: You'll go to an auto detailer, who will take Q-Tips to the brake pedal and toothbrushes to the spaces between the radio buttons. Your car will be as sparkling as the day you bought it.

Detailers' prices range from \$40 to more than \$300, with \$150 standard for the full treatment. For the fastidious, the difference between a regular car wash and an excellent detailing job is as apparent as the difference between a Yugo and a Ferrari. All too often, though, the service isn't as lofty as the price.

In choosing a top-flight detailer, look first for experience. Don't be surprised if half the detailers in the phone book are no longer in business. When you find one, insist on seeing the shop. "It should look like a hospital and be run like the military," says Stephen Grisanti, president of Classic Shine Auto Fitness Centers, a nine-shop chain based in Greenwich, Conn.

HAND-BUFFED. Ask to inspect a finished car. Of course, it will have been pampered with an exceptionally thorough cleaning, waxing, and buffing. So you're looking for the points that divide first class from business class. Are the underside of the trunk lid, the wheel wells, and the inside of

the gas cap clean? Did the tailor take the spare tire and clean it? Any dust in air vents? Has all wax been removed from all cracks, jams, and under the hood? Any burn marks along an edge, say, left by an overzealous orbital buffing? Auto tonier shops eschew power buffers entirely, preferring to do all polishing by hand.

You should be treated well as your car is. It means a shuttle service between the shop and your office. Finding the right detailer involves effort, but the sparing just might make time, at least, seem spent.

Jim

Worth Noting

- **JUMP START.** Sign ahead, and National Rental lets you bypass the desk at airports in San Francisco, Los Angeles, and Jose, Calif. An ATM accept credit cards and issues keys. The system is set for 50 other airports in 1989.
- **GOLF DATA.** The 500+ *Golf Digest Almanac* comes with a one-hour video highlights of 48 men's events during 1988. The set is \$50 from *Golf Digest*, Box 60, Indianapolis, Ind. 46268.
- **TAX GOOF.** Misled by the IRS? Noting the name of the clerk who fielded your phone call can ward off a penalty.

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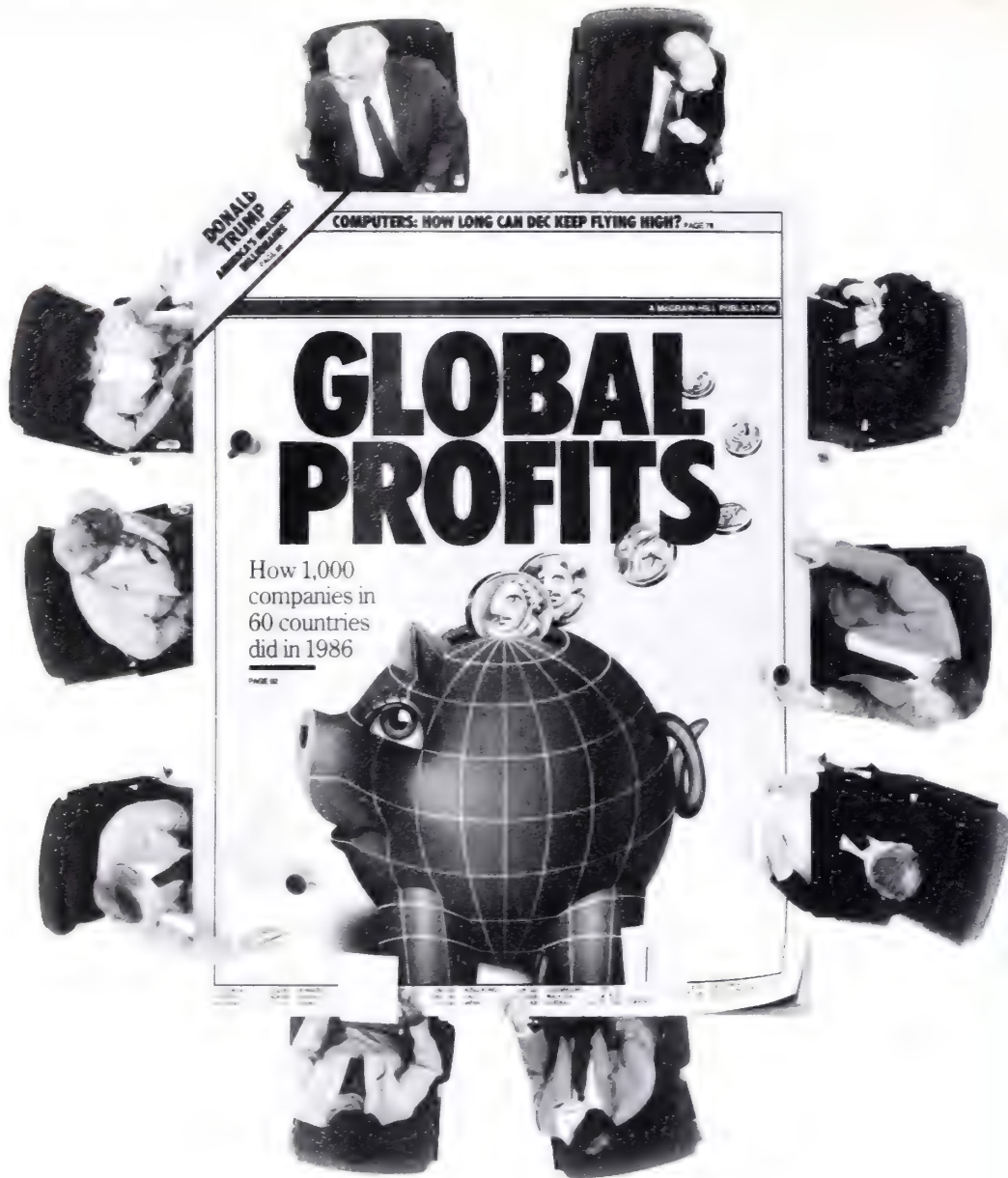
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Index to Companies

gives the starting page for a story or feature. Significant reference to a company. Most companies are indexed under their own names. Companies listed only in tables are not included.

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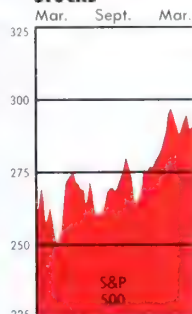
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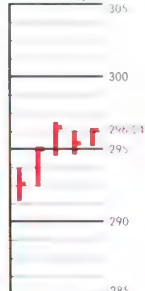
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STOCKS



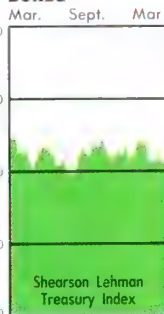
52-week change
11.6%

Mar. 30-Apr. 5



1-week change
1.3%

BONDS



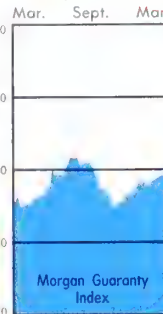
52-week change
-2.7%

Mar. 30-Apr. 5



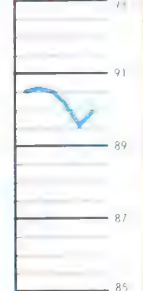
1-week change
+0.8%

THE DOLLAR



52-week change
4.8%

Mar. 30-Apr. 5



1-week change
-0.7%

STOCK ANALYSIS

SECTORS	Latest	% change Week	% change 52-week
INDUSTRIALS	2304.8	1.0	11.8
FINANCIALS (Russell 1000)	156.8	1.4	11.7
TECHNOLOGICALS (Russell 2000)	158.5	1.1	11.5
UTILITIES (Russell 3000)	168.5	1.4	11.7

STOCKS	Latest	% change (local currency) Week	% change (local currency) 52-week
FINANCIAL TIMES 100	2078.2	0.3	19.1
NIKKEI INDEX	33,360.8	1.9	25.8
DOW JONES COMPOSITE	3556.1	-0.1	5.8

FUNDAMENTALS

	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	9.1%	9.3%	6.2%
30-YEAR TREASURY BOND YIELD	9.0%	9.1%	8.8%
S&P 500 DIVIDEND YIELD	3.5%	3.7%	3.4%
S&P 500 PRICE/EARNINGS RATIO	11.9	11.8	15.3

TECHNICAL INDICATORS

	Latest	Week ago	Reading
S&P 500 26-week moving average	283.3	282.4	Positive
Stocks above 26-week moving average	58.4%	55.5%	Neutral
Speculative sentiment: Put/call ratio	0.21	0.29	Negative
Insider sentiment: Vickers sell/buy ratio	1.36	1.31	Positive

INDUSTRY GROUPS

LEADERS	% change 4-week	% change 52-week
CENTER BANKS	13.8	42.2
	10.1	39.9
	9.6	25.7
STRUCTURED HOUSING	8.7	41.0
TELECOMS	7.1	34.7

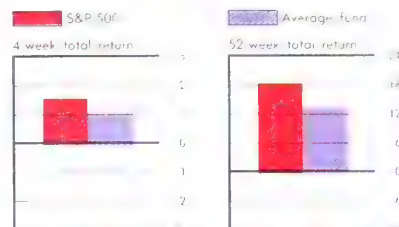
LAGGARDS	% change 4-week	% change 52-week
TECH	-13.2	-1.4
ENTERTAINMENT	-7.0	-15.5
BUILDING	-6.7	30.1
MINING	-6.6	3.6
	-6.4	22.7

Strongest stock in group	% change 4-week	% change 52-week	Price
CHASE MANHATTAN	17.2	49.3	37 1/2
CIRCUS CIRCUS ENTERPRISES	15.2	31.7	36 7/8
WESTMORELAND COAL	25.4	8.2	19 3/4
SKYLINE	18.2	30.0	19 1/2
PEPSICO	7.6	27.1	44 1/2

Weakest stock in group	% change 4-week	% change 52-week	Price
FEDERAL EXPRESS	-14.0	-2.7	45 1/8
HEWLETT-PACKARD	-7.4	-15.2	51 1/2
KAUFMAN & BROAD	-32.2	12.3	10 1/4
NEWMONT MINING	-10.7	12.0	38 5/8
INCO	-10.7	16.0	28 1/8

MUTUAL FUNDS

total return	%	LAGGARDS	Four-week total return	%
GIC INVESTMENTS	9.5	STRATEGIC GOLD/MINERALS	-9.0	
SERVICES GOLD SHARES	9.1	FIDELITY SELECT COMPUTERS	-4.7	
GLOBAL STRATEGIC HEALTH SCIENCES	8.7	MERRILL LYNCH PACIFIC B	-4.0	
total return	%	52-week total return	%	
ANN	63.0	STRATEGIC GOLD/MINERALS	-22.1	
CAPITAL APPRECIATION	37.9	STRATEGIC INVESTMENTS	-22.0	
BIA SPECIAL	35.3	STEADMAN OCEANOGRAPHIC TECHNOLOGY	-15.9	



RELATIVE PORTFOLIOS

Investment	Value	Change
Foreign stocks	\$12,307	+3.33%
U. S. stocks	\$11,732	+1.28%
Treasury bonds	\$10,676	+1.71%
Money market fund	\$10,659	+0.16%
Gold	\$8,521	-1.05%

This page is as of market close Wednesday, Apr. 5, 1989, unless otherwise indicated. Data include S&P 500 companies only; performance and share prices are as of market close.

Apr. 4. Mutual fund returns are as of Mar. 31. Relative portfolios are valued as of Apr. 4. A more detailed explanation of this page is available on request.

KEEP THE MILKEN CASE IN PERSPECTIVE

The indictment of Michael R. Milken in the biggest criminal securities fraud case ever deserves the attention it is receiving. Surely a major attraction in this case has been the sheer heft of the bankrolls involved. Milken, who was paid \$550 million in 1987, deserves a special award for 1980s-style excess. That, however, is not the real issue. Milken is charged with extremely serious crimes: stock manipulation, insider trading, and other fraudulent activities. The grand jury said that Milken's firm, Drexel Burnham Lambert Inc., realized \$206 million in investment banking fees and \$38 million in trading profits over a two-and-a-half year period from deals tainted by illegal acts.

The size of the numbers involved has tended to blur perspective on this astonishing case. Most of the investment banking fees earned by Drexel were not the result of illegal acts, but incidental to them. The indictment suggests Drexel did not reap much more than \$50 million from allegedly illicit doings, certainly a lot of money but no more than a tiny percentage of Milken's and Drexel's total income. So even if all the charges are true, they do not establish that the takeover or deal process on Wall Street has been corrupted. They do not establish systemic corruption. Nor can it be shown that many people were hurt.

Compare the Milken case with three other scandals in the news. We have the savings and loan mess, which could cost taxpayers as much as \$150 billion. The General Accounting Office has said that the pattern of fraud and abuse was "pervasive" and was the chief cause of the crisis. In the penny stock scandal, many firms were corrupt to the core, as were the markets they made. The extent to which they rigged markets was vastly more blatant than anything alleged against Milken. And in the Pentagon procurement scam, the entire process by which the Defense Dept. obtains weapons was corrupted. Again we have systemic abuse.

Milken shouldn't be left off the hook without a fair trial. He is accused of doing some very bad things. On the other hand, his notoriety made him an obvious target. But in parceling out our scarce resources for fighting white-collar crime, far more systemic abuses that are clearly harming taxpayers or investors cry out for greater attention.

THE U.S. NEEDS MORE TRADE TALKS WITH JAPAN

A crucial decision point is at hand in U.S.-Japanese relations. Under the 1988 Trade Law, the Bush Administration must identify the unfair trading practices of foreign nations by Apr. 30. By May 31 it must pick countries to start negotiations on ending those practices. Retaliation could eventually follow. Tokyo is arguing that fingering Japan as appropriate for such talks would signal a sea change in U.S.-Japanese relations. Worse, they say, it

could topple Prime Minister Noboru Takeshita, already in from the Recruit Co. bribery scandal.

These arguments must be considered. But Japan's billion trade surplus with the U.S. can't be ignored. It is the largest that any country holds and the most persistent. Of course, the U.S. budget deficit, our high-dollar policy of the 1980s, sluggish productivity growth, and relative lack of product quality bear much of the blame. Still, the market has been far more open to Japanese products than vice versa.

It would be foolish to identify a smaller country such as South Korea as a priority nation while ignoring Japan. Japan would figure rightly that the U.S. is willing to pick on the small guys but not willing to wrestle with the giant. Nor is the argument about Takeshita very persuasive. Japan's governmental structure would remain in place.

The trade law was designed to spur Washington to come to grips with the trade problem. American officials should use discretion in selecting targets. There's no reason, for example, to take on the explosive issue of Japanese electronics when the sales opportunities for Americans are relatively small. Better to demand more cash registers ringing from sales of American microchips and construction services.

HOW INCOME INEQUALITY ROBS AMERICA

The gap between the rich and the poor usually deepens in good times, as a booming economy offers more jobs and pay hikes to those on the bottom rungs of society. It hasn't turned out that way during the 1980s. Reaganomics has brought us the longest boom in 40 years. But ironical inequality has steadily widened.

In part, this seems to stem from the nature of the 1980 recession. Industries with high-paying jobs, such as autos and autos, suffered severely as the U.S. economy was thrown open to serious world competition for the first time. Even though many of the companies adapted and are now profitable again, many became competitive through savings or higher productivity. This reduced the number of high-paying jobs normally generated during recoveries.

Unfortunately, there are longer-term trends at work, such as the growth in the number of single mothers and the advent of two-earner couples. In addition, slow productivity growth has stunted the growth of wages, which after adjustments for inflation are barely higher than they were 15 years ago. This has hit lower-paid workers hard, boosting inequality even as the economy recovers.

Young workers have fared badly. Because they're usually the last hired, they're usually the first fired. And their wages aren't growing. The upshot is that their children are more likely today to grow up in poor families. The dearth of this is causing an education and skill levels has long-term implications for the U.S. While most people disagree on the gross inequality on moral grounds, the economic corollaries may be even more disturbing. As more children and young people fall behind, we are not replenishing our stock of human capital.

BusinessWeek

APRIL 24, 1989

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GAMBLING FEVER

Is It Good
for Us?

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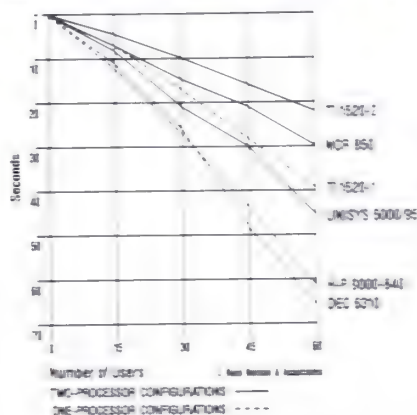
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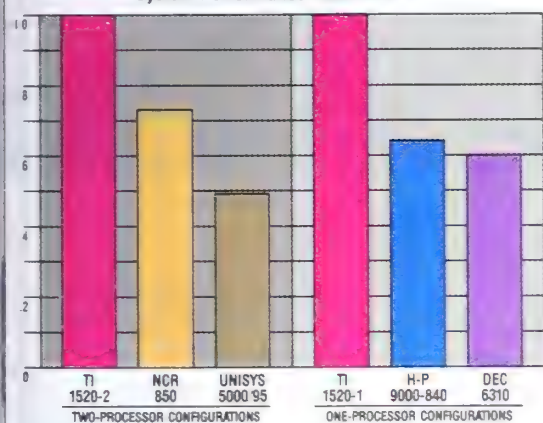
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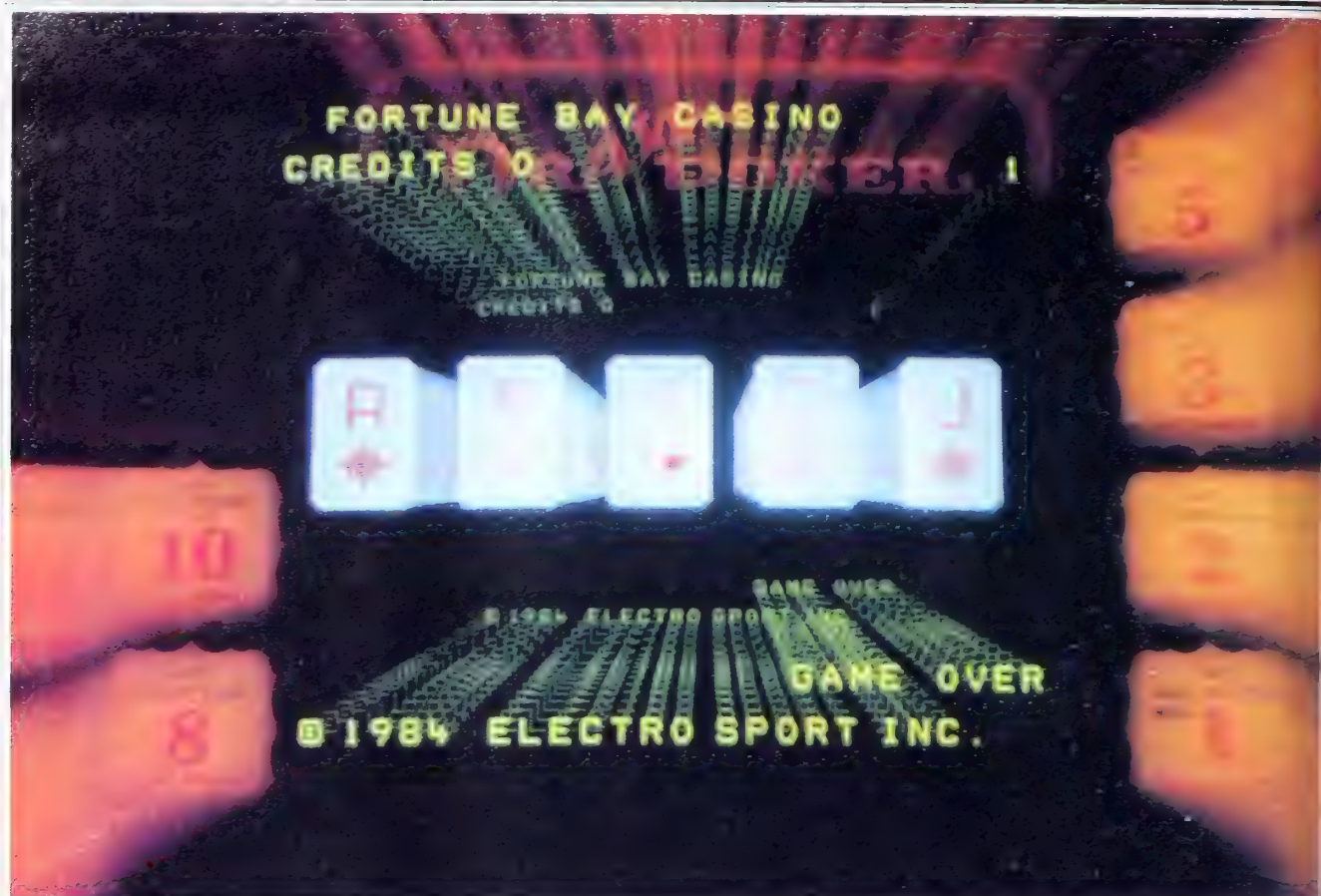


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WANNA BET? VIDEO POKER MACHINES ARE THE HOTTEST THING IN ONE OF AMERICA'S BIGGEST GROWTH MARKETS—LEGAL GAMBLING

Cover Story

112 GAMBLING FEVER

From the swanky hotels of Las Vegas and Atlantic City to the lottery agent on the corner, Americans everywhere are scrambling for a piece of the action—or a shot at a pie-in-the-sky fortune. And state and other local governments increasingly are looking to gambling as a sure thing in the battle against budget shortfalls. But is this good for us?

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The expansion may be headed for a fabled soft landing

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New heir-apparent Allan Gilmour will be looking for a partner

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GLQ223 appears to kill the virus—and shield healthy cells from harm

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HP's merger with Apollo puts it ahead of DEC and Sun—for now

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Slim now, G&W is looking for media companies to gobble

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A CROWDED WILDERNESS:
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Wright's travails rattle Congress

THIS LAND IS WHOSE LAND?

The government is taking heat for mismanagement of public lands

A HOUSE DIVIDED AT INTERIOR

Accusations and bickering are rife

The Corporation

NORTHROP UNDER FIRE

A 167-count indictment is the latest blow to the B-2 bomber's maker

FOUR SEASONS AT THE BEACH

The pricey hotel chain is diving into the waters of plush resorts

Finance

THE ESOP TIE-IN

Companies are linking performance with pensions

CHASING NORTHWEST

Financiers Checchi and Wilson are old partners in dealmaking

WALL STREET'S NEW LOVE

The use of 'soft dollars' to buy information is spreading

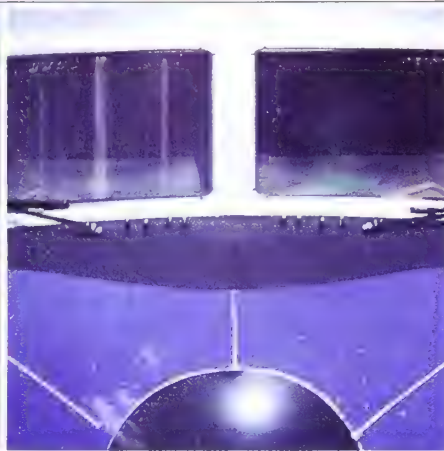
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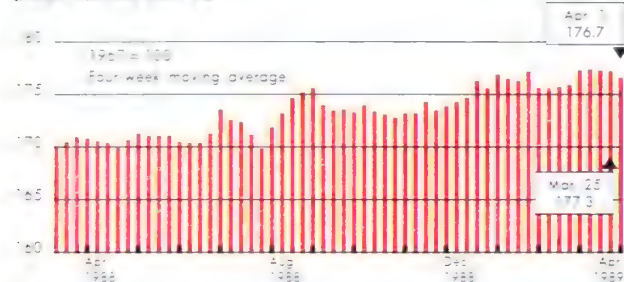
Don't make the U. S. one big casino
Congress shouldn't pamper ESOPs
Are S&Ls getting another easy ride?

BusinessWeek Index

PRODUCTION

Change from last week: -0.3%

Change from last year: 3.2%



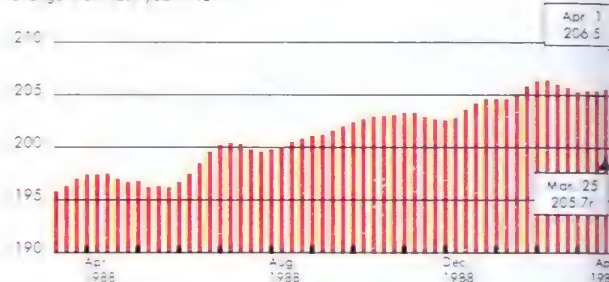
The production index fell for the week ended Apr. 1. On a seasonally adjusted basis, output of autos, trucks, and coal plunged. Smaller declines were posted in steel, electric power, lumber, and paper output. Rail-freight traffic, paperboard, and crude-oil refining production increased for the week. Before calculation of the four-week moving average, the index fell to 175.7 from 176.7 in the previous week. For March, the index increased to 177, from 176 in February.

BW production index copyright 1989 by McGraw-Hill Inc.

LEADING

Change from last week: 0.4%

Change from last year: 4.5%



The leading index rose sharply for the week ended Apr. 1. This week's increase returns the index to its level prior to the three-week decline posted in February. For the latest week, higher stock prices, fewer business failures, and faster growth rate in materials prices, real estate loans, and M2 offset slightly higher bond yields. Prior to calculation of the four-week moving average, the index increased to 208.3 from 206.8. In March the index rose to 206.3, from February's 205.7.

Leading index copyright 1989 by Center for International Business Cycle Research

PRODUCTION INDICATORS

	Latest week	Week ago	% Change year ago
STEEL (4/8) thous. of net tons	2,029	2,030	= 4.1
AUTOS (4/8) units	160,166	130,416r	= 25.0
TRUCKS (4/8) units	87,180	75,117r	= 17.8
ELECTRIC POWER (4/8) millions of k. watt-hours	50,692	49,132	= 8.3
CRUDE-OIL REFINING (4/8) thous. of bbl./day	12,998	13,449r	= -0.5
COAL (4/1) thous. of net tons	19,318	19,896	= -0.2
PAPERBOARD (4/1) thous. of tons	772.1	757.3r	= 0.9
PAPER (4/1) thous. of tons	757.0	758.0r	= -1.2
LUMBER (4/1) millions of ft.	482.6	483.4	= -4.6
RAIL FREIGHT (4/1) billions of ton-miles	19.9	19.2	= -0.6

Sources: American Iron & Steel Inst., Ward's Automotive Reports, Edison Electric Inst., American Petroleum Inst., Energy Dept., American Paper Inst., WWPA, SFPRA, Association of American Railroads.

FOREIGN EXCHANGE

	Latest week	Week ago	Year ago
JAPANESE YEN (4/12)	133	132	124
GERMAN MARK (4/12)	1.89	1.87	1.66
BRITISH POUND (4/12)	1.89	1.70	1.88
FRENCH FRANC (4/12)	6.37	6.31	5.64
CANADIAN DOLLAR (4/12)	1.19	1.19	1.23
SWISS FRANC (4/12)	1.67	1.64	1.37
MEXICAN PESO (4/12)	2,406	2,397	2,315

Sources: Major New York banks. Currencies expressed in units per U.S. dollar, except for British pound expressed in dollars.

PRICES

	Latest week	Week ago	% Change year ago
GOLD (4/12) \$/ounce	387.250	383.000	-13.8
STEEL SCRAP (4/11) = 1 heavy, \$/ton	115.50	118.00	-2.9
FOODSTUFFS (4/10) index, 1967 = 100	224.1	225.5	2.3
COPPER (4/8) c/lb.	135.7	143.4	20.4
ALUMINUM (4/8) c/lb.	93.5	93.5	-19.4
WHEAT (4/8) = 2 hard, \$/bu.	4.36	4.48	40.8
COTTON (4/8) strict low middling 1-1/16 in., c/lb	59.51	58.79	1.4

Sources: Chicago Board of Trade, Chicago Merc. Commodity Research Bureau, Metals Week, National Wheat Producers Assn.

LEADING INDICATORS

	Latest week	Week ago	% Change year
STOCK PRICES (4/7) S&P 500	296.08	292.38	1
CORPORATE BOND YIELD, Aaa (4/7)	9.81%	9.88%	
INDUSTRIAL MATERIALS PRICES (4/7)	104.9	104.9	
BUSINESS FAILURES (3/31)	228	297	-2
REAL ESTATE LOANS (3/29) billions	\$317.0	\$316.1r	1
MONEY SUPPLY, M2 (3/27) billions	\$3,089.0	\$3,082.4r	
INITIAL CLAIMS, UNEMPLOYMENT (3/25) thous.	317	322	

Sources: Standard & Poor's, Moody's, Journal of Commerce (index: 1980=100), Dun & Bradstreet (failures of large companies), Federal Reserve Board, Labor Dept. (CIBCIR seasonally adjusts data on business failures and real estate loans).

MONTHLY ECONOMIC INDICATORS

	Latest month	Month ago	% Change year
BUSINESS WEEK PRODUCTION INDEX (Mar.)	177.0	176.0r	
BUSINESS WEEK LEADING INDEX (Mar.)	206.3	205.7r	
EMPLOYMENT, CIVILIAN, MILLIONS (Mar.)	117.1	116.9	
UNEMPLOYMENT RATE, CIVILIAN (Mar.)	5.0%	5.1%	-1

Sources: BW, CIBCIR, BLS

MONETARY INDICATORS

	Latest week	Week ago	% Change year
MONEY SUPPLY, M1 (3/27)	\$787.1	\$786.9r	
BANKS' BUSINESS LOANS (3/29)	312.0	312.1r	
FREE RESERVES (4/5)	104.9	128r	7
NONFINANCIAL COMMERCIAL PAPER (3/29)	111.6	112.9	3

Sources: Federal Reserve Board (in billions, except for free reserves which are expressed in two-week periods in millions)

MONEY MARKET RATES

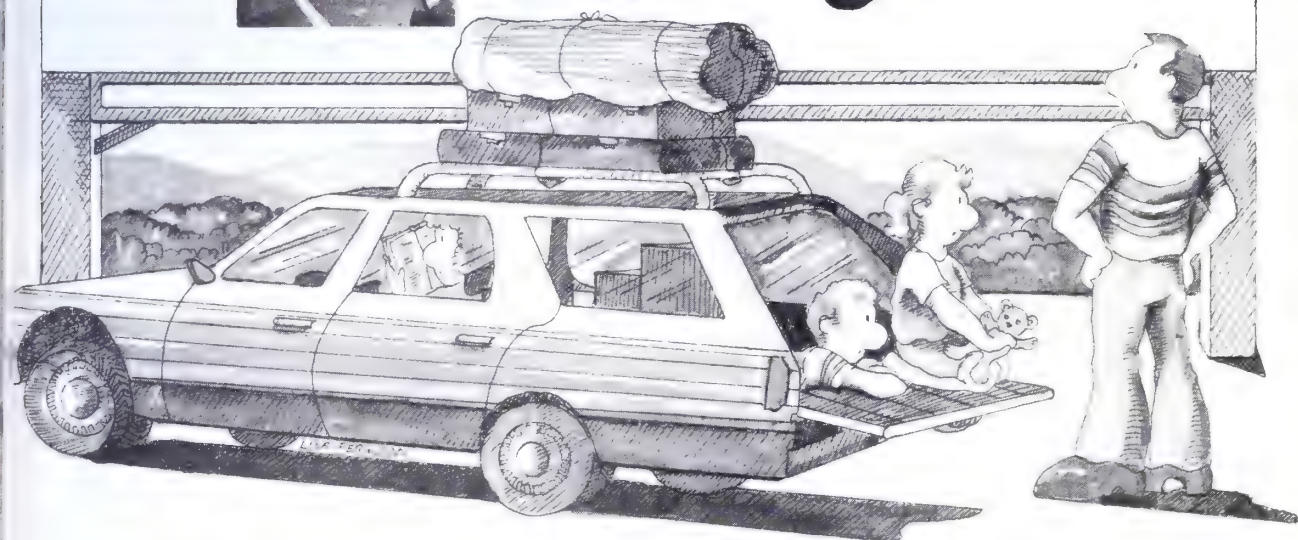
	Latest week	Week ago	% Change year
FEDERAL FUNDS (4/11)	9.79%	9.52%	6.8
PRIME (4/12)	11.50	11.50	8.5
COMMERCIAL PAPER 3-MONTH (4/12)	9.88	9.87	6.8
CERTIFICATES OF DEPOSIT 3-MONTH (4/12)	10.05	10.00	6.8
EURODOLLAR 3-MONTH (4/5)	10.14	10.31	6.8

Sources: Federal Reserve Board, First Boston

1 = Western Wood Products Assn. 2 = Southern Forest Products Assn. 3 = Free market value NA = Not available r = revised NM = Not meaningful



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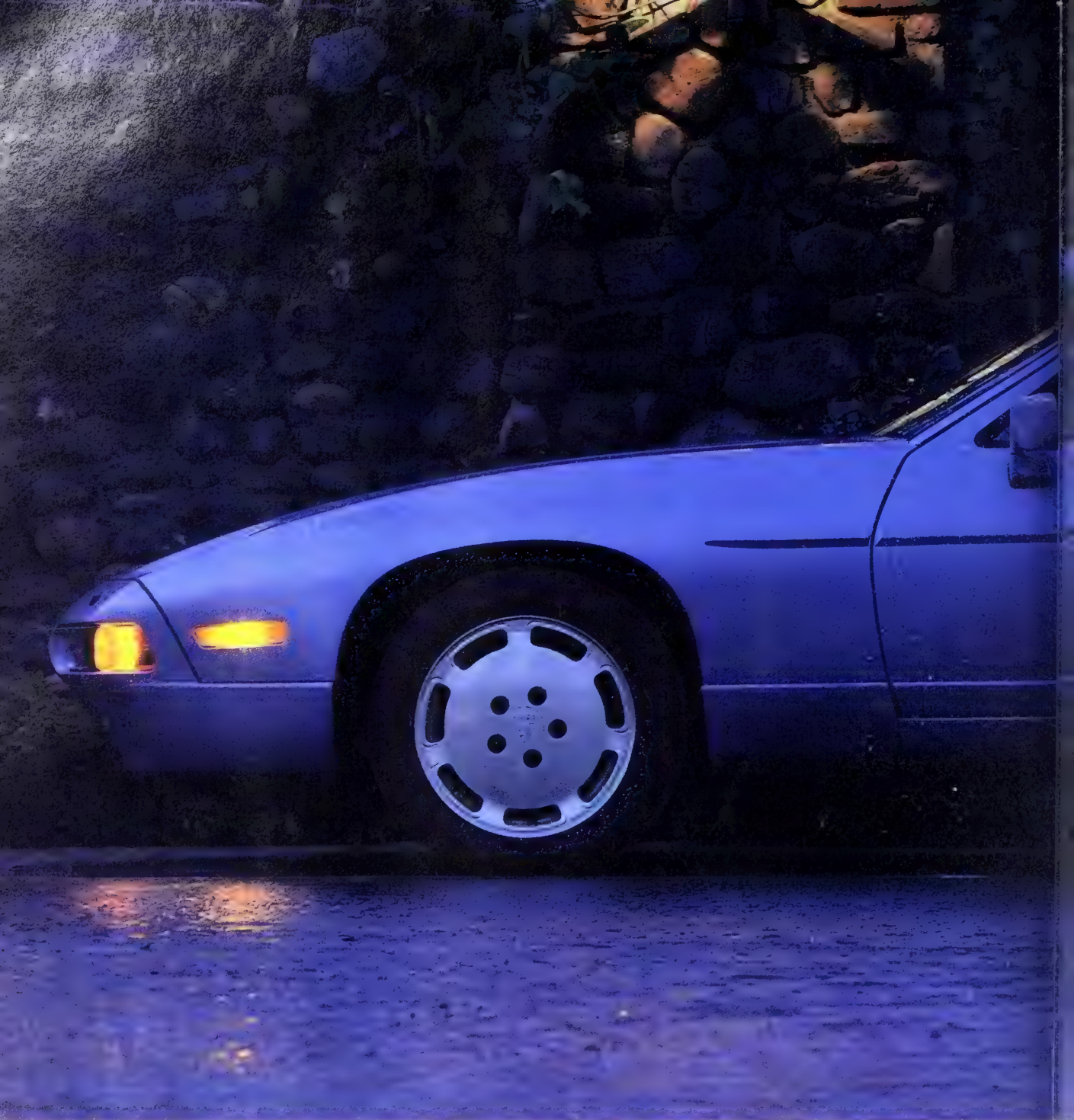


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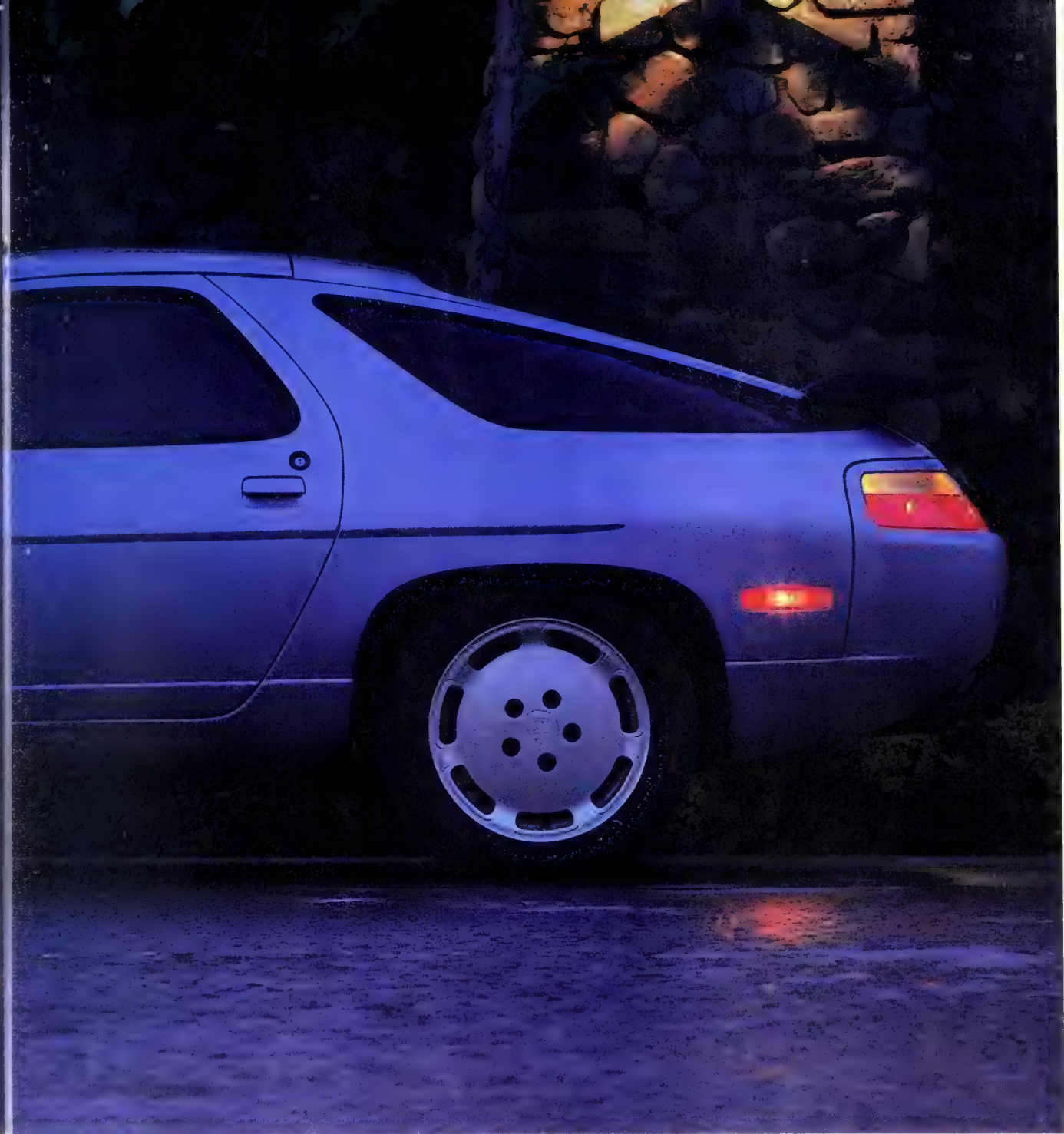
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PORSCHE



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Creative Director, Bloomingdale's

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CORRECTIONS

se lips can be expensive" (In Business Week, Mar. 27) stated that insider-trading charges had been against William S. Banowsky, a ty Corp. director. In fact, the Securities & Exchange Commission filed charges against him on Mar. 14. Bany settled them, without admitting any guilt, by paying \$754,000.

use a stock split was not accounted for, the Corporate Scoreboard (Mar. 27) was off by a factor of two in listing earnings per share and the price-earnings ratio of MCN Corp. The correct figures are \$2.32 and 7.5 respectively. Also, the company's total annual earnings were misstated because the outdated data used for the tables included dividends on preferred stock, and a subsidiary, Michigan Consolidated Gas Co., pays the preferred dividends, not MCN. Thus earnings for the year were actually up 18%; earnings for 1988 as a whole were \$47.7 million, up 5%; and 1988's return on equity was 19.4%.

and the many states you mentioned, not for the federal government?

George Ronay
Los Angeles

ON UNIVERSITY SAYS IT'S INTO EACH FOR THE LONG HAUL

Our recent article "At Boston University, Biotech 101 is no breeze" (of the News, Apr. 10), is shoddy. A report "BU rushed into such a venture because . . . it hoped to sell quickly." BU rushed into nothing. A partial stockholder in Seragen Inc. since its founding in 1980, BU acquired a controlling interest in 1987 after thorough and exhaustive deliberation, and intend to increase our interest because of its prospects as a highly valuable investment. Our expectation that we could finance some of the development costs through an early IPO ended with the stock market crash of 1987. But our proposed IPO was not a vehicle for the company; it was a well-established means to bring fresh capital into the company.

The article distorts the relative importance of our investment in Seragen. BU's total operating budget is not \$110 million as reported, but \$540 million. Our expenditure on research at Seragen is \$10 million annually. That is in addition to more than \$200 million (including \$100 million received from outside sponsors) expended annually for all other re-

search at BU. In other words, Seragen represents only about 6.5% of the amount we spend on research each year—and less than 2.5% of the University's annual operating budget.

Seragen's research has as its goal saving the lives of some 25,000 people in the U.S. alone who would otherwise die of incurable cancer. If BU should spend \$13 million each year for the next four years and as a result save 25,000 lives a year, it will be a magnificent achievement.

Seragen's business plan projects that before the end of the century, the company will be generating a net annual income of more than \$400 million. Our present holdings, now in excess of 76%, might be somewhat less by then—but very substantial nevertheless.

In fact, Boston University's intention is not to cash out but eventually to cash in. And whether we cash in financially or not we have every reason to believe that we shall have helped save thousands of human lives.

John Silber, President
Boston University
Boston

Editor's note: We regret the error about the size of the university's operating budget. Otherwise, we stand by the story, and it remains to be seen whether or not Boston University's large spending on a high-risk venture ever pays off.

BOYD JEFFERIES IS SORELY MISSED

Thank you for your story about our company ("Life after Boyd? And how," Finance, Mar. 20). While we appreciate your mentioning how well our firm has done in the past two years, we are concerned with the impression that we are happy that Boyd Jefferies is no longer with us.

We obviously regret the circumstances that led to Boyd's departure. He did make mistakes and has taken responsibility for them. That should not detract, however, from the fact that we are grateful to him as our founder, for all that he did for the company and for our employees. His spirit of maximum service to our clients continues to inspire us.

Frank Baxter, President
Jefferies & Co.
New York

Letters to the Editor should be sent to Readers Report, Business Week, 1221 Avenue of the Americas, New York, N.Y. 10020. Fax: (212) 512-6875, Telex: 12-7960, Intl. 4998204. All letters must include an address and daytime and evening telephone numbers. We reserve the right to edit letters for clarity and space.

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DODGE DYNASTY: THE CAR AND THE FAMILY THAT ROCKED DETROIT

By Caroline Latham and David Agresta
Harcourt Brace Jovanovich • 360pp • \$19.95

FROM PIONEERS OF INDUSTRY TO BICKERING SOCIALITES

In 1903, when the buyers of Henry Ford's first cars put their money down, they did so with the reassuring knowledge that they were buying a product built primarily by Dodge Brothers. If they knew Ford at all, it was as a racing-car developer whose companies had failed. But John and Horace Dodge—that was different. That same year, Ransom Olds's curved-dash Oldsmobile accounted for about 30% of the 11,000 cars built in the U.S., and Dodge Brothers had supplied all of Olds's transmissions. Dodge stood for quality, reliability, and durability.

The first half of *Dodge Dynasty: The Car and the Family That Rocked Detroit* is a fascinating account of how the hardworking Dodges rode the automobile boom to fantastic riches. John and Horace, the youngest of a mechanic's

five children, grew up working on boat engines. Highly skilled engineers with an intense drive to improve any device they got their hands on, they developed a dust-resistant bearing for bicycles and eventually founded their factory in Detroit. The contract with Olds, won in 1902 when their company was scarcely a year old, gave them their first big break.

They were in their late 30s when Henry Ford approached them with plans for a car featuring a new engine configuration—its twin cylinders would be set in the engine block vertically instead of horizontally. Horace insisted on making other changes in the engine and rear axle before taking on the job.

Even then it was a risky contract. Dodge Brothers would build all of the car's mechanical parts, with Ford adding only wheels, rubber tires, and a rather

inelegant wooden body with upholstered seats. John and Horace not only financed their own expansion to fill the order but also soon became investors in the struggling Ford Motor Co. That willingness to take the risk, and to pay all their profits back into their factory, paid off. That first Ford was the Model A. John, Horace, and Henry were on the road to enormous success.

The Dodges enjoyed the journey. They raced power boats together—a passion of Horace's—and built successively grander homes. Who shared them, however, was a persistent source of turmoil. The resentment between Horace's wife, Anna, and John's third wife, Matilda, played a large role in spoiling the happiness of future Dodge generations.

Meanwhile, the business grew, and it did friction with Ford. Henry Ford gradually drove out all the other initial shareholders in Ford Motor, but his dependence on Dodge Brothers as a supplier undermined his control. When the conflicts came to a head, the Dodges split from Ford in 1913 with an estimated joint net worth of \$50 million. They would build their own car, the first equipped with a steel body. Their effort won a singular endorsement: Lieutenant

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George S. Patton Jr. used dodges rather than horses in raid on one of Pancho Villa's commanders. In 1915, its first year manufacturing cars, Dodge Brothers built 45,053. In 1920 it built 145,000, closing in on Ford and the new General Motors Corp. But John and Horace didn't live to enjoy the full fruits of their vision. With an almost eerie incidence of illnesses, both died before the year was over. If the first part of *Dodge Dynasty* is the two brothers' rags-to-riches tale, the second is the money-doesn't-buy-happiness saga of their heirs. After John and Horace died, the company was split between their estates, and in 1925 their heirs sold it for \$146 million to an investment bank, in part to sever the unpleasant tie between Anna and Matilda. The two women then launched a lengthy social and spending competition, and they and their children bickered over shares of the family trusts. Horace's will left the income from his estate to Anna, with the principal to go to their children after her death. But Anna's grip on the purse strings was matched



HORACE AND JOHN DODGE: NOT SO GOOD AT ENGINEERING FAMILY LIFE

only by her grip on life. When she died in 1970, at 98, the two children were already dead. While they lived, she manipulated them by controlling their allowances, and they responded by staying stuck in adolescence: One of Horace Jr.'s ex-wives claimed that when he was well into his 50s, he once stood on the roof of a Palm Springs open-air restaurant and urinated on the Duchess of Windsor.

Such engaging yet sorry anecdotes

make up *Dodge Dynasty's* too-long second half. Money bought the brothers' heirs a lot of marriages, a lot of divorces, and a lot of contested wills. Authors David Agresta, a Detroit native who was intimate with the Dodge circle, and Caroline Latham, who has written about a number of celebrities, describe every incident in numbing detail.

For the Dodges in the 30s, life was like a Shirley Temple movie—the Depression never happened. But later generations were ill-equipped to manage their wealth or build useful careers. Some raced boats and bred horses; others seemed to do little more than drink in plush surroundings.

The Dodge heirs rarely practiced philanthropy, and the family name has faded from public consciousness: The brand survives only as a division of Chrysler. This book gives Horace and John their due. But the descent that fills its second half is the ironic fate of a family that lived the American Dream.

BY JAMES B. TREECE

Jim Treece is BUSINESS WEEK's Detroit bureau manager.

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ECONOMISTS REALLY SHOULD GET OUT MORE OFTEN

BY ROBERT KUTTNER



Formal economics has long practiced a learned myopia toward human and social realities. But now even mainstream economists are beginning to acknowledge that theory doesn't make the world go round

The story is told of two economists crossing the street. "Look," says one, "there's a dollar bill on the sidewalk." The other replies: "No, there isn't." The first insists: "Yes, there is." The other says, "No. If it were a dollar bill, somebody would have picked it up."

The joke rubs in an oft-heard criticism of the economic method: In formal economics, deductive reasoning tends to crowd out empirical inquiry. For example, monopolies supposedly don't matter much because some competitor soon must come in and undercut the high price. Japanese industrial policy didn't make any constructive difference because it couldn't have. Some individual acts may seem altruistic, but by definition they must be merely special forms of self-gratification. And so on. Thus are apprentice economists taught to perceive the world and spared the need to investigate its complexity.

For decades this brand of learned myopia has given other social scientists hives, but challengers have made few inroads within economics. In a profession that resolves issues by definition, epistemological heresies neatly define the challenger as a noneconomist. Suggest that perhaps industrial policy does some good, and you might make the op-ed page of *The New York Times*, but you won't get tenure.

A couple of weekends ago, however, some 250 social scientists gathered at Harvard business school in the hope of founding a new branch of the social sciences: "socioeconomics." The meeting, convened by sociologist Amitai Etzioni, brought together historians, legal scholars, sociologists, anthropologists, social psychologists, professors of management, and even a few economists.

DEPTH PERCEPTION. Socioeconomics questions the assumptions of orthodox economics in several respects. It challenges the simple behavioral assumption that people "maximize their utility" by pursuing selfish gratification. In Etzioni's recent book, *The Moral Dimension*, he shows that human motivation reflects not only egoistic impulses but also some received ethical framework about what is good or necessary for the collectivity. Says Etzioni: "Economics does great damage by teaching 3 million students a year that to be selfish is to be efficient. To call everybody who doesn't follow that behavior irrational is to condemn the human race."

The socioeconomic approach also insists that economic phenomena be appreciated as existing in both a social context and in "historic time," where the physical-science analogy of equilibrium that so appeals to economists does not readily apply because history is not revers-

ible. The meeting included a testimonial dinner honoring four social scientists who have long practiced socioeconomics "without even knowing it," as teased Etzioni: economists Albert Hirschman of Princeton's Institute for Advanced Study, Amartya Sen of Oxford and Harvard, Harvey Leibenluft of Harvard, and sociologist Neil Smelser of the University of California at Berkeley. In their work, all have insisted on a more complex conception of human motivation and an understanding of economic behavior as socially mediated.

The conference treated such issues as the rights of corporate "stakeholders" vs. shareholders in takeovers and reorganizations; how organizations in different societies adapt to technological change; why market economies must be understood as creations of society and not as "natural" occurrences; and social explanations for why some economies develop and others stagnate.

LOOSENING UP. At one session Harvard Professor Emeritus Ray Vernon, a distinguished international economist and a veteran of battles with economic orthodoxy, expressed pessimism that academic economics departments would ever be receptive to the heresies of socioeconomists. But one can identify instructive cracks in the dike of economic orthodoxy in the recent work of some eminently mainstream economists.

Massachusetts Institute of Technology Professor Paul Krugman's new view of international trade acknowledges that in a global economy of imperfect competition, national policies may serve to shift profits from one national economy to another. Empirical work by Harvard economist Lawrence Summers finds that actual wages in different occupations reflect custom and history as well as "marginal productivity." Studies by Berkeley's George Akerlof explain social explanations for why employers find it necessary to pay workers wages in excess of what would "clear the market." And Harvard's Jeffrey Sachs has criticized the destructive role of private banks in the economics of Third World debt.

In each of these cases a mainstream economist wrestles with social, institutional, or political factors, acknowledging that private markets are complicated by social imperatives and, by themselves, do not necessarily optimize outcomes. So the new discipline of socioeconomics may find some allies even among economists. It's high time. Economists ought to descend from the realm of theory and appreciate the fascinating and messy world of human intercourse. They should pick up that dollar bill. Adam Smith would approve.

ROBERT KUTTNER IS ECONOMICS
CONTRIBUTOR FOR THE NEW REPUBLIC
AND AUTHOR OF THE LIFE OF THE PARTY

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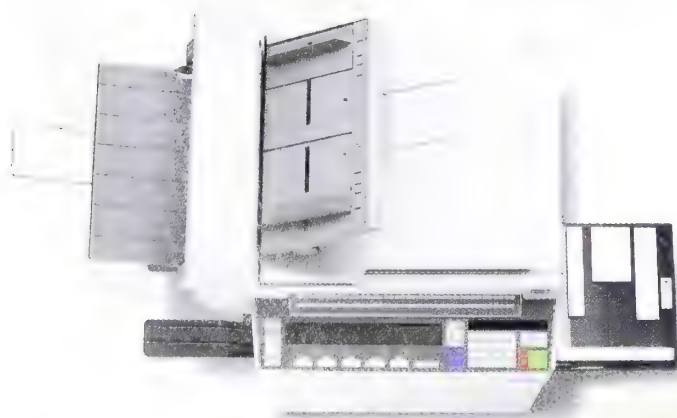
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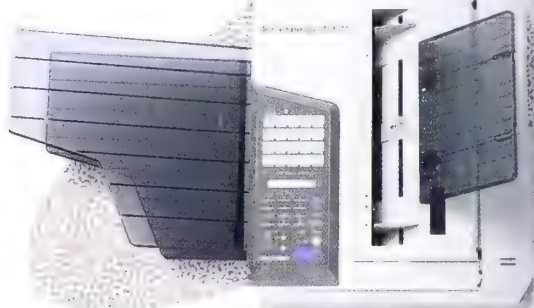
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BY MICHAEL J. MANDEL

WHY STOCKS GET WEAKER AS INFLATION GETS STRONGER

Who's afraid of 5% inflation? Stock-market investors are—and with good reason. Since 1960, in years when inflation has been 4% or less, total real returns on stocks have averaged almost 12% annually. But once prices start rising faster than 4%, the returns from stocks fall sharply (chart). Indeed, when inflation ranges from 4% to 7%—these days it's running at about 5%—the average real rate of return on stocks plunges to only 1.2%.

Economists have long had a hard time explaining this link between high inflation and poor stock market performance. Since stocks are claims on the earnings and assets of companies, they should theoretically provide a good hedge against inflation. As prices rise, earnings generally follow suit, and so, too, should stock prices. For this reason,

HOW INFLATION HURTS THE MARKET



▲ PERCENT
* AVERAGE FOR THE YEARS 1960-88, ADJUSTED FOR INFLATION;
INCLUDES CAPITAL APPRECIATION AND DIVIDENDS
DATA: IBBOTSON ASSOCIATES

some economists suggest that what really hurt stocks in the inflation-ridden mid-'70s was not the rise in the general price level but the nasty effects of OPEC's price hikes on the industrial sector.

However, David P. Ely of San Diego State University and Kenneth J. Robinson of the Federal Reserve Bank of Dallas recently presented evidence to the contrary in the bank's *Economic Review*. They found that there was still a link between inflation and a weak stock market in the early 1980s. When inflation began to subside in 1982, the stock market started its ascent.

Why can't the market tolerate high inflation? Ely argues that investors anticipate that the Fed will clamp down in

response to inflation, perhaps sending the economy into a recession. Jason Bendorly of Goldman Sachs & Co. agrees, noting that "when inflation rises, [monetary] policy is going to tighten and potential corporate profits next year will be lower." Bendorly points out that sustained inflation also lowers aftertax profits this way: Since capital-depreciation deductions are based on original cost, inflation cuts the value of depreciation allowances and raises the tax bite.

According to Ely and Robinson, the stock markets in other countries—including, notably, Japan—are just as sensitive to inflation. So with inflation rising almost everywhere, stocks around the globe may be in for tough sledding.

DID TAX REFORM FILL THE PROFIT NUMBERS WITH HOT AIR?

Three years and one Presidential election have passed since the tax reforms of 1986, and many of their effects are only now beginning to show up. Take corporate profitability. In 1988 reported aftertax corporate profits rose by a healthy 12.7%—the largest increase since 1983.

But in reality the tax changes may have created an image of false robustness. According to Christopher Caton of DRI/McGraw-Hill, much of last year's profit increase merely reflects the changing rules for depreciation. Under the old rules, companies were able to depreciate their capital investments faster, reduce taxable profits, and thereby have more cash flow at their disposal. But by slowing the depreciation rate, the 1986 tax reforms shifted a portion of corporate income into profits—an apparent gain that simply subjects more income to taxes. Under the new tax rules, Caton notes, "the effects of the transition will be over by 1992."

Until then, to get a more accurate picture of profits, says Caton, it's better to use aftertax profits from current production and thus remove the distorting effects of the tax changes. By this measure, profits last year increased by only 3.5%, barely keeping up with inflation.

DON'T EXPECT ANY CAPITAL-GAINS TAX CUT TO NOURISH STARTUPS

Will lowering the capital-gains tax unleash a surge of funds for investment in new ventures, as the Bush Administration has argued? Probably

not, says James M. Poterba of Massachusetts Institute of Technology. In a recent paper, Poterba reports that out of the \$4 billion invested in venture capital funds in 1987, less than 15% came from individuals who would benefit from a cut in the capital-gains tax. Instead, about half of venture funding came from tax-exempt pension funds and nonprofit institutions, with the rest supplied by corporations and foreign investors unaffected by the tax rates that individuals face.

Although a lower capital-gains tax won't raise the supply of venture funds, it could make starting a new business more attractive, Poterba concedes. He notes that capital gains are a key part of the compensation of entrepreneurs and other employees of startup companies, so a cut in the capital-gains tax might make people more willing to undertake new ventures. But even if it did, reducing the capital-gains tax across the board would be like using a cannon to shoot a fly. In 1987, Poterba calculated, venture capital accounted for less than 1% of all realized capital gains, making nonventure capital assets the main beneficiary of any cut in capital gains rates.

TEXAS IS BOUNCING BACK—WITHOUT OIL AS A SPRINGBOARD

The Texas economy is finally climbing out of a deep 10-gallon hat. A year ago the state was suffering from a 7% unemployment rate, but since then the Texas rate has fallen to 6%, not far above the national average of 5%. Ad recent reports from the Conference Board and Merrill Lynch & Co. suggest that the state is overcoming the collapse of the oil industry. The rise in oil prices to the \$20-a-barrel level hasn't undone the damage in the oil patch, but it was counting on an energy revival to bring Texas back. Indeed, observes Steven R. Malin of the Conference Board, "the Texas economy is more diverse than it has been in 15 years."

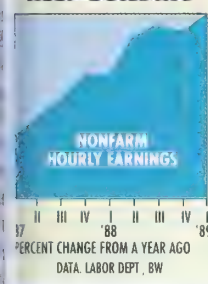
And although the working-age population in Texas is still declining, the Merrill Lynch report predicts that by the end of the year, Texas will again see a net influx of people from other states. Housing starts and construction should revive.

Longer-term, says Merrill Lynch, low-wage labor from Mexico will help Texas attract new manufacturing jobs. But there's one hitch: As Texas banks and thrifts continue to hemorrhage, businesses in the state may have trouble raising the capital they need to expand.

AS THE EXPANSION WEARS ON, BUSINESS FACES BIGGER BILLS

After nearly six-and-a-half years, the economic expansion is finally beginning to act its age. Tight labor markets and high rates of capacity utilization have forced the Federal Reserve Board to raise interest rates to contain inflation. That's a classic picture of the late stage of a business cycle.

WAGE PRESSURES KEEP BUILDING



For companies, that means the cost of doing business is escalating. The March report on the job markets made it clear that labor costs are accelerating. Hourly earnings last quarter rose 4% over the past year—up from 3% a year ago and 2% the year before that (chart).

Most of the wage pressure is in services. Hourly earnings in manufacturing are up only 3.1%

from last year. That's about in line with gains in factory productivity, so factory unit-labor costs are still tame. But in the service-producing industries—where 76% of nonfarm workers are employed—the job-weighted average of wage rates is up 4.4% over the year. Productivity gains there have been dismal, which means that unit-labor costs are skyrocketing.

Moreover, the first quarter of 1989 marked the first time in eight-and-a-half years that producer prices of consumer goods other than food and energy outpaced costs at the consumer level. And those cost pressures are still rising: The widely followed index of raw-material prices published by the *Journal of Commerce* hit a new high for the week that ended on Apr. 7.

CORPORATE PROFITS WILL TAKE HIT

It's not just raw materials and labor that are putting on the squeeze. Higher interest rates drive up the cost of corporate debt and drain cash flow (profits plus depreciation allowances). In the fourth quarter, interest payments of nonfinancial companies rose to 21.3% of cash flow. That's close to the record 22.7% hit during the '3-74 recession. Rising rates last quarter doubtless shed the ratio even higher.

The growth of cash flow itself is getting squeezed because depreciation is waning as the government phases out the liberal deductions allowed in the early '80s. So companies have fewer internally generated funds for current operations and for capital spending. Capital spending plans, at least for the first half of '89, are quite ambitious. The Commerce Dept.'s latest survey shows that companies will increase their outlays

for new plants and equipment by 9.1% this year, to \$469 billion, compared with 10.3% last year. Adjusted for price changes, Commerce pegs this year's real increase at a slower 6.3%, compared with 10.1% in 1988.

Even so, Commerce projects that real outlays will grow at an 11.2% annual rate in the first half, an acceleration from the 3.2% pace in the second half of last year. With cash flow waning, companies will have to take on even more debt to see those plans through.

As costs continue to rise, the pressures will ultimately hit corporate profits. First-quarter earnings at many companies likely felt the pinch, and the outlook isn't bright, especially if demand weakens further.

Some companies have been able to hold up their bottom lines by passing along higher costs through higher prices. But the more Fed tightening cuts into the growth of demand, the more companies will feel the pressure. The economy could even end up with a nasty combination of sluggish growth and higher inflation.

THE LABOR MARKETS GET EVEN TIGHTER

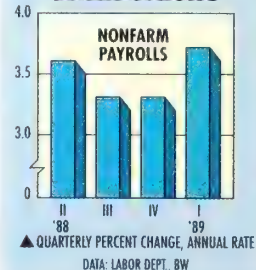
Clearly, growth in demand is the key to the business outlook. The latest message from the labor markets is that the props under domestic demand remain firm, but slower growth in foreign demand is beginning to dampen gains in manufacturing. This shows up in the recent pattern of job growth.

Nonfarm industries added 180,000 workers in March. That was the smallest gain in seven months, but it has to be seen against the background of a 280,000 increase in February and a 424,000 jump in January. Job growth in the first quarter was unusually volatile, particularly in construction, because of exceptional weather patterns.

The March increase was pulled down by a drop of 49,000 jobs in construction after a 22,000 decline in February. But construction employment had soared 107,000 in January. Despite weakness in residential building, the February and March declines are probably overstated. Construction jobs aren't likely to fall that much in April. Also, the strike at Eastern Air Lines subtracted about 25,000 workers from the transportation sector, but those jobs will return.

Looking at the entire first quarter gives a truer picture of job growth. Nonfarm employment last quarter rose at a 3.7% annual rate (chart), the fastest pace in a

JOB GROWTH STILL LOOKS STRONG



Business Outlook

year. But job growth in manufacturing is losing steam.

Factories added only 18,000 workers in March, after an 11,000 drop in February and a 53,000 rise in January. Even with the big January gain, job growth in manufacturing slowed to a 1.9% annual rate last quarter, from 2.8% in the fourth quarter. That slide reflects the sharp slowdown in export growth since mid-1988.

The factory workweek fell in March, to 40.9 hours, from 41.1 hours in February. That's still fairly high, but any further deterioration would be a sure sign that factories are scaling back operations.

However, the service sector remains buoyant, and that's a good sign for domestic demand. Jobs in service industries rose at a 3.9% annual rate last quarter, up from 3.5% in the fourth quarter. So services are still generating jobs and incomes at a rapid clip.

That's one reason the outlook for consumer spending is still bright. Nonfarm personal income has grown faster than consumer outlays for two consecutive quarters. In addition, the ever-tighter labor markets can only lift consumer confidence. That means the slowdown in consumer spending last quarter isn't likely to last.

The civilian jobless rate fell to 5% in March, the lowest since December, 1973. In fact, that tightness is drawing in workers from fringe areas of the job markets. In the first quarter, the number of people working part time because they couldn't find full-time work continued to fall. Adjusted for labor-force growth, the number is the lowest in eight years. And discouraged workers—those who have dropped out of the work force because they feel they cannot find a job—hit a nine-year low.

INCOME OUTPACED RISING CREDIT

With the job markets so strong, it's not surprising that consumers are still willing to add heavily to their installment debt.

Installment credit in February grew by a strong \$4.2 billion, following a \$4.4 billion addition in January. The February gain pushed total credit out-

standing to a high of \$674.8 billion. That's 8.1% above its level of a year earlier (chart).

And with income gains still on solid ground, the rapid mounting of debt isn't likely to slow anytime soon. In fact, since December, disposable income growth has actually outpaced increases in installment credit. So consumers have plenty of resources to boost their credit purchases.

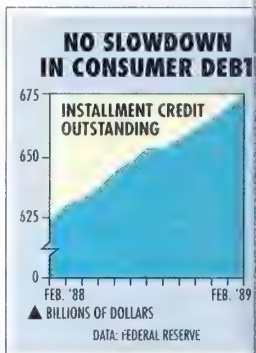
The ratio of debt to disposable income dipped to 18.2% in February. That ratio has edged down since its record peak of 18.9% in April, 1988, but it's still historically high. And there are few signs that consumers are worried about buying on credit.

The continued surge in revolving credit, which includes credit cards, personal loans, and lines of credit from banks, indicates the opposite. It grew by \$1.6 billion in February. In the past year it has expanded by 15.2% compared with 5.5% for all other installment debt.

Auto loans have also been surprisingly strong, despite weak car sales. That's because sales of light trucks haven't suffered as much. In January and February, consumers bought new trucks at a 4.1 million annual rate—about equal to the 4.2 million pace of 1988. And since truck-price increases have outpaced those of cars recently, loans to buyers are larger.

March truck sales did fall to a rate of 3.8 million, but car sales were so weak in the first quarter that domestical-made trucks still captured a record 29.2% of the market for all vehicles sold in the U.S.

With job gains so strong and consumer confidence high, people are likely to keep buying on credit. For now that will help businesses cope with rising costs. But it also means that inflation will probably get worse.



THE WEEK AHEAD

CONSUMER PRICE INDEX

Tuesday, Apr. 18, 8:30 a.m.

The consensus is that consumer prices increased 0.5% in March, following a 0.4% rise in February. A drop in new-car prices and financing costs partly offset higher food and energy costs last month. This suggests that consumer prices in the first quarter probably rose at an annual rate of 5.4%—the highest quarterly gain in five years. The quicker March pace is likely to upset inflation-wary financial markets.

HOUSING STARTS

Tuesday, Apr. 18, 8:30 a.m.

New-home construction in March probably declined to an annual rate of 1.45

million. That's indicated by a drop in housing permits in February and a fall in construction employment in March. Rising mortgage rates and high home prices are hurting the construction sector. In February, housing starts stood at an annual rate of 1.5 million.

REAL EARNINGS

Tuesday, Apr. 18, 10 a.m.

Average weekly earnings for nonfarm private workers, after adjustment for inflation, most likely dropped by 0.1% in March. An expected 0.5% increase in the CPI for urban wage earners will more than offset the 0.4% increase in average hourly pay. Inflation-adjusted earnings have been losing ground since 1984. Workers may well try to make up for

this loss in purchasing power now that labor markets are so tight. That could put greater upward pressure on wages and inflation. In February real earnings fell 0.6% from January—and 1.3% from a year earlier.

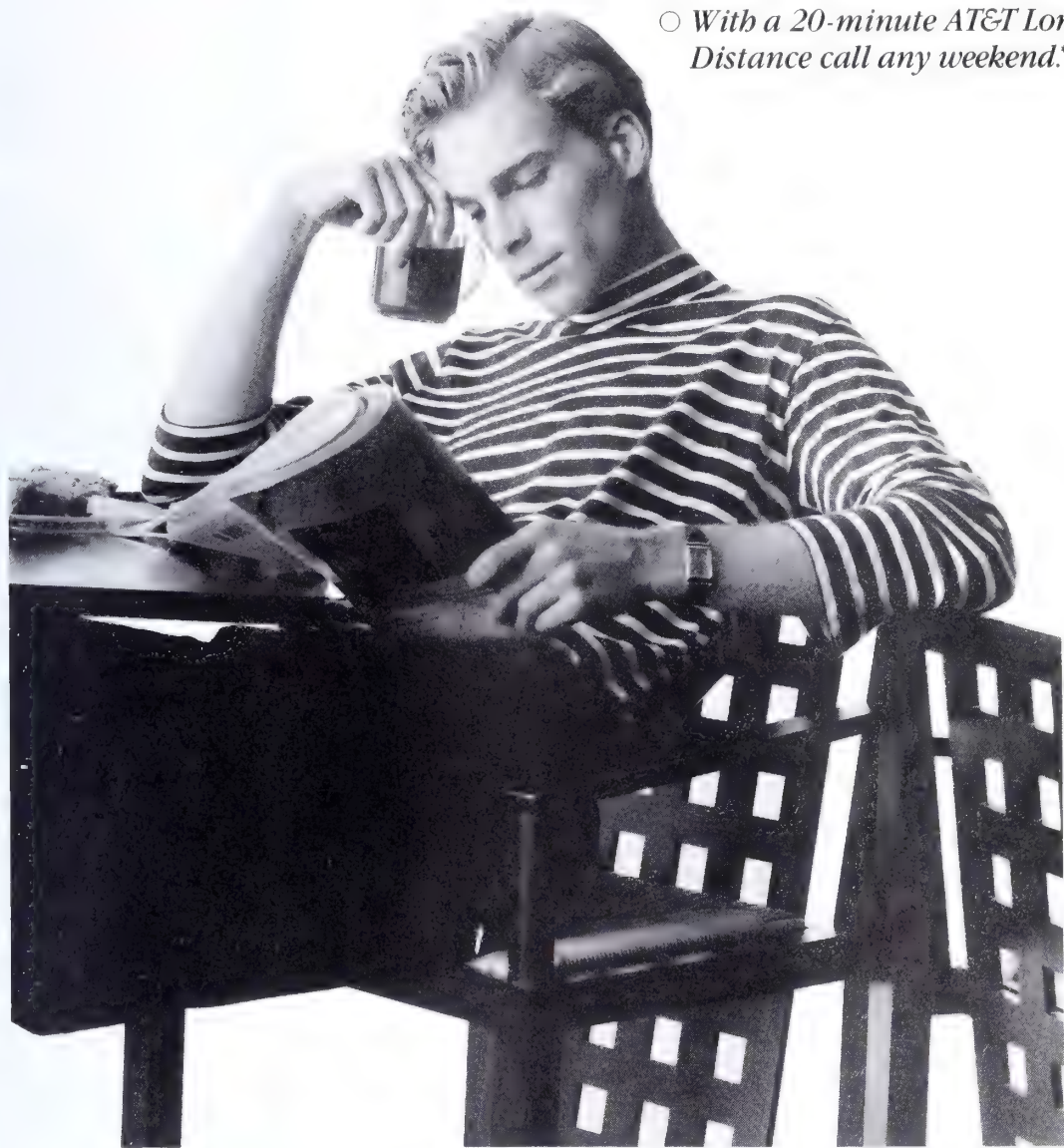
FEDERAL BUDGET

Friday, Apr. 21, 2 p.m.

The federal government will probably report a \$35 billion deficit for March. In March, 1988, the budget gap tallied \$29 billion. Most economists expect that government spending increased last month while tax receipts were unchanged. So far in this fiscal year, the deficit totals \$92.7 billion, compared with \$90.3 billion accumulation for the same period last year.

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HOW LORENZO'S DEAL WITH UEBERROTH COLLAPSED

He's the golden boy from Newport Beach, the man with the Midas touch, the magician who turned the Olympics into a profitable proposition and swept baseball into megaprofitability. But not even Peter V. Ueberroth, capitalist wizard, could bring Eastern Air Lines Inc.'s fractious interests together in a deal to pull it out of its descent into liquidation.

After six days of grueling negotiations that had him shuttling between New York, Washington, and Los Angeles, Ueberroth on Apr. 12 announced that his tentative deal to buy Eastern from Frank Lorenzo's Texas Air Corp. for \$464 million "is finished, it's terminated, it's over." The deal, Ueberroth explained, had foundered on the unions' insistence that Texas Air immediately hand control of Eastern over to a court-appointed trustee—a condition flatly rejected by Lorenzo.

Lorenzo didn't show up for the midtown Manhattan press conference. But Eastern President Philip J. Bakes vowed to press on with a new plan of "rebuilding a smaller Eastern Air Lines" and flying it out of Chapter 11 bankruptcy proceedings where the Miami-based carrier is now grounded. "We're disappointed," he said. "We tried very, very hard."

PILOT PINCH. Texas Air will need more than hard effort to make that vision a reality. Although scaled back, a leaner Eastern would still field about half the carrier's prestrike schedule of 1,040 flights a day and roughly half its former work force of 31,000 (table). But this strategy seems implausible on its face, given the unions' steadfast refusal to

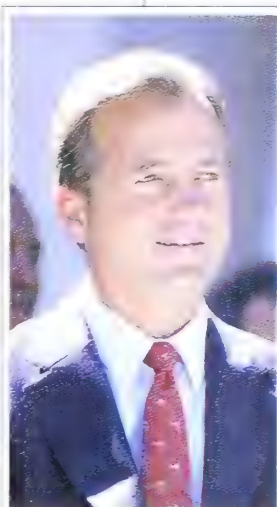
work for Lorenzo and a federal judge's Apr. 12 ruling that the pilots' strike is legal. Right now, Eastern has just 4,500 workers running 116 flights a day. "I don't think you can shrink an airline to profitability," says Shearson Lehman Hutton Inc.'s airline specialist Robert J. Joedicke. "Bakes must foresee hiring off the street. But unless he hires some off the strike lines, he will have a hard time getting pilots."

More likely, Texas Air wants to convey the impression that it still has a plan that U.S. Bankruptcy Judge Burton R. Lifland could find acceptable. Lifland has insisted that Eastern get its planes airborne again—and soon. A strategy to revive Eastern as a smaller carrier would show that Texas Air is heeding Lifland's demand in good faith and that a more drastic solution—liquidation—isn't needed.

MARATHON MEN. Sources within Ueberroth's group say they still hold out hope of taking control of the airline one day. They suggest that Lifland might eventually appoint a trustee after Lorenzo has a chance to present his case in a court hearing on the trustee question. By that time, they suggest, the airline's situation would be that much bleaker and the carrier might be gotten that

much cheaper.

Failing that, buyers probably will return with new offers. They could include Ueberroth or Chicago investor Jay Pritzker. "We're still probably in the best position because we have an understanding with the unions," says a Ueberroth confidant. And Trans World Airways Inc. owner Carl C. Icahn says he's still interested. "I don't think there is



Ueberroth says his bid for the carrier 'is finished, it's terminated, it's over'





any real common equity left" in Eastern, Icahn said in a statement. "Therefore, although I might be willing to risk my capital in Eastern, I would not be willing to pay it over to Texas Air." Instead, Icahn said he would only bargain with the unions and creditors toward a merger of Eastern and TWA.

ABOUT-FACE. That Pritzker, Icahn, and even Lorenzo would still figure in Eastern's future seemed a remote prospect on the morning of Apr. 10. Ueberroth thought he finally had clinched his deal for Eastern. After a marathon, 24-hour session run by David I. Shapiro, the examiner appointed by the bankruptcy court, the carrier's three unions agreed to give Ueberroth the concessions he needed. Bleary-eyed, the whole group boarded a morning Pan Am shuttle flight from Washington to New York: the union leaders, Ueberroth, Shapiro, and former Defense Secretary Frank C. Carlucci, whom Shapiro wanted as a trustee to run Eastern. They all filed into Judge Lifland's lower Manhattan chambers and told him of their success. He agreed to appoint Carlucci. The happy crew went around the corner to a small restaurant for lunch.

But when they returned, Lifland had changed his mind after Texas Air had objected strenuously to anyone's taking control of Eastern before he was paid. He and Ueberroth had fought over this issue days earlier and put it aside. Shapiro had agreed to ask the judge for a trustee only because the unions—in particular, the leader of the machinists, Charlie Bryan—insisted that they wouldn't work for Lorenzo.

Lifland then told Lorenzo and Ueberroth to work it out without a trustee. They tried all day Apr. 11. It didn't work, and their deal expired at midnight. "The judge did a 180-degree turn, and Ueberroth's deal died," says one insider. Adds Harvey R. Miller, a Texas Air lawyer: "You can't take away Texas Air's assets without due process. We haven't had a hearing yet." Lifland called the lawyers back to his chambers the next morning for one more try, but no one budged.

The issue of Lorenzo's control has plagued the Ueberroth deal from the very start. The many on Ueberroth's

team, union officials, and Texas Air insiders who were interviewed for this story say the labyrinthine tale began last November, when Eastern's unions first met the then-baseball commissioner in his New York offices. Ueberroth told them that Lorenzo had just that week offered him a job running Eastern. The matchmaker: Minnesota Twins owner Carl R. Pohlad, who also sits on Texas Air's board.

Pohlad had been leaning on Lorenzo for a year to sell Eastern. Ueberroth told the unions that he had declined the job offer, saying he would only get involved with labor's support. But the unions remained suspicious that he might be secretly in league with Lorenzo and Pohlad. "Dealing with Lorenzo has been like a house of mirrors," says one union strategist. "We don't know who's on whose side."

After Eastern's union struck on Mar. 4 and the carrier a few days later filed for bankruptcy, Lorenzo told Ueberroth he was ready to sell. Ueberroth then

began discussions in earnest with the unions about the concessions he wanted. But the unions insisted that Lorenzo get out. They feared that even if Ueberroth wasn't a secret Lorenzo ally, he was being used as a stalking horse to get them back to work. After the 60 to 90 days it would take to get Eastern out of bankruptcy and transferred to Ueberroth, Lorenzo might back out of the deal and keep Eastern, they worried. Ueberroth and Lorenzo went around and around on this point. Finally, Lorenzo agreed to pay a \$20 million fee if he reneged. Still, the unions remained dissatisfied.

Pritzker, whose wealthy Chicago family recently sold Braniff Inc., then made an offer, but it, too, fell apart. So Lorenzo began talks with Ueberroth again and his partner, J. Thomas Talbot, a former airline investor and neigh-

bor from Newport Beach. Talbot suggested a compromise. The unions would return to work under Lorenzo during the interim period. But they would sign contracts that expired the day the sale to Ueberroth closed. If Lorenzo backed out, the unions would revert to their prestrike pay scales. And over the next three years their wages would go up. In addition, Lorenzo agreed not to sell as-



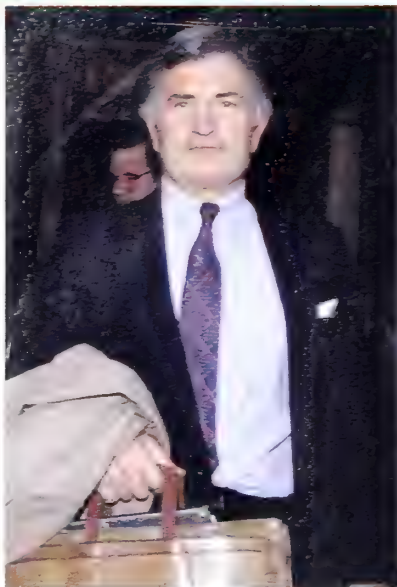
Lorenzo wants to rebuild a smaller Eastern and fly it out of bankruptcy

Top of the News

sets or change

Talbot's proposal... Ueberroth and Lorenzo—but again, not the unions. Their lawyers said if the Ueberroth deal fell through after they had returned to work, they'd be in an awkward legal position even if the interim contracts expired. At that point, Shapiro suggested a trustee.

Why did Lifland get cold feet about appointing a trustee? Several reasons. Even if all Lorenzo really wanted was a shot at keeping Eastern, he did have a point about first getting his money. If a trustee took over, Lorenzo would have little more clout than any other Eastern creditor. And if Ueberroth's management team ran the airline during bankruptcy and did a poor job, the trustee might decide that the company couldn't afford to pay Lorenzo



BANKRUPTCY JUDGE LIFLAND AGREED TO APPOINT A TRUSTEE, THEN RENEGED

law firm not involved in Eastern litigation. But in this case, Lifland would be equating business reasons with what he sees as the public's interest in getting the planes flying again. Says Goldman: "That would be the first time this was done."

All day on Apr. 11, Lifland tried to resolve the dilemma. Sources close to the talks say that Lorenzo suggested they speed up the deal so it would close in 10 days. That way he would get his money and there would be no need for a trustee. Then Lorenzo reversed himself and asked for 30 days. Lifland tried to persuade Ueberroth to go along, to no avail. "The airline would waste away and wouldn't be worth as much money," says a source close to Ueberroth.

Tempers ran short. At one point, Miller allegedly said to Robert J. Rosenberg, one of Ueberroth's lawyers, that Ueberroth's objection could be overcome

nation's most prominent bankruptcy lawyers. Miller is said to have warned Lifland, who has presided over such high-profile cases as the Manville Corp. and LTV Corp. bankruptcies, that he could set a dangerous precedent by appointing a trustee. Under the bankruptcy laws, there are drawn-out procedures for selling the entire assets of a company. They can be skipped if there are "overriding business reasons," notes William M. Goldman, a bankruptcy expert at Brown & Wood, a

if Lorenzo could lower his price by \$1 million. Rosenberg told others about the idea, those present say, but apparently hadn't been cleared with Texas Air.

A short time later, Rosenberg and several of the principals were standing in the judge's chambers, with Lifland nearby. Miller, a large man, strode up to Rosenberg, allegedly grabbed him by the necktie, and, according to an eyewitness, said: "Don't you ever say Harry Miller said anything again." Miller declined to comment on the incident.

MILKEN PRESSURE. By 7 p.m., Lifland asked Ueberroth, Talbot, Lorenzo, and Bakes to come into his chambers. They talked for half an hour, then Lifland sent the four off to try one last time. "We came back at 9 o'clock and said we couldn't do it," said one person involved. "Lorenzo wouldn't turn over the management of the company."

Ultimately, Lorenzo probably will have to let go of Eastern anyway. Insiders say he didn't really want to sell

the first place, to Ueberroth or anyone else. But Pohlad, another Texas Air officer, had been pressuring him for nearly a year. Pohlad says he told Lorenzo: "Either we work it out [with the various unions], or maybe we'd better sell it."

Lorenzo had been getting pressure last year from Michael R. Milken, the Drexel Burnham Lambert Inc. junk bond king who now faces a 98-count federal racketeering indictment in the Wall



TALBOT SUGGESTED AN INTERIM COMPROMISE

Street scandal. Drexel has backed Lorenzo financially since 1985. But Milken, who for years had been a neighbor of Ueberroth, says he also began telling Lorenzo and Ueberroth that the commissioner was the right guy to take the helm at Eastern. Shortly after the war out began, Milken called Ueberroth and offered to fund his bid.

To Lorenzo, that had to hurt. But even as he gave in to pressure, he kept looking for a way to remain in control. He has. And he has held on to Eastern with all the odds against him. But the longer he keeps his grip, the less Eastern's worth. That's a trend Eastern's creditors are unlikely to tolerate much longer.

By Aaron Bernstein and Christopher Power in New York, with Gail DeGeorge in Miami, Todd Vogel in Houston, and Ed Schine in Los Angeles



THE IAM'S BRYAN BALKED AT A DEAL WITH LORENZO

ment saying they were concerned about the Ueberroth team's apparent lack of a detailed business plan. The creditors—suppliers and equipment makers such as Airbus Industries—were worried that Lorenzo had made off with too many of Eastern's assets. If Ueberroth had a harder time than he expected getting Eastern flying again, debt-holders could wind up with less than full payment on their IOUs.

BAD PRECEDENT. Lifland had other reasons for tabling the plan for a trustee. When Ueberroth's crew went to lunch that Monday, insiders say that the judge

HOW EASTERN HAS SHRUNK

	1988	1986
	Dollar figures in millions	
TRAFFIC*	28.86 billion	34.9 billion
DAILY FLIGHTS	1,040	1,500
AIRCRAFT	257	286
EMPLOYEES	31,000	39,000
REVENUES	\$3,500	\$4,400
OPERATING INCOME	-\$209	\$65
NET WORTH	-\$201	\$319

* Miles flown by paying passengers
DATA: COMPANY REPORTS

** Pre-strike

RE WE HEADED FOR THE FABLED SOFT LANDING?

Washington does its job, the coming slump could be brief and shallow

After 6½ years of faithful service, the economic expansion is beginning to sag. But unlike recent expansions, this one probably won't end in a sudden collapse. Instead, prices will rise, and the Federal Reserve Board will continue to keep a tight hold on the money needed to fuel further growth. Consumers may temporarily lose their appetite for buying anything that isn't on sale. Expanding inventories will lead to layoffs. And production will slow. Already, factory orders are declining (see chart) and inventories of some big-ticket goods are creeping upward. The unemployment rate has dropped to 5%, and the cost of everything from wages to commodities is drifting higher. If that sounds like the textbook end to a classic business cycle, it is. It has been that way since the U.S. economy has suffered such a turn that analysts may no longer know one when they see it. After the 1981-82 recession came virtually overnight, after the Federal Reserve effectively shut down the economy in an effort to get inflation under control. Before that, the recession of 1980 resulted in a series of horrendous policy mistakes by the Carter Administration. And the 1973-74 downturn was largely the result of the Arab oil embargo. This year's slowdown is unlikely to be as dramatic. American Enterprise Institute economist John Makin, who predicts a recession late this year, says it will be a light out of Econ 101. "What we are

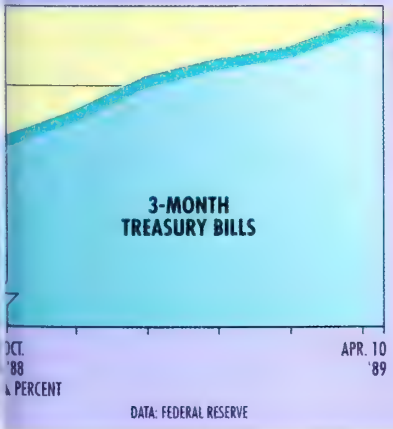
seeing," Makin says, "is a fairly conventional end to the business cycle." That means the downturn will develop gradually, perhaps imperceptibly. And because the slow-motion slowdown will give policymakers plenty of time to react, the length and depth of the slump could be largely controlled by Washington's response. If the government does its job, the coming slump could be shallow and relatively brief. For now, the Bush Administration has no visible strategy for fighting a recession, other than to deny that one is imminent. Fiscal policy hinges on another time-buying budget agreement with Congress that will do little to reduce the actual borrowing needs of the federal government. That leaves both inflation-fighting to the Fed, which has proved very good at the former and not very adept at the latter. With just the right amount of fine-tuning, Fed Chairman Alan Greenspan could continue to walk the line between inflation and recession. But as price

'What we are seeing,' says one economist, 'is a fairly conventional end to the business cycle'

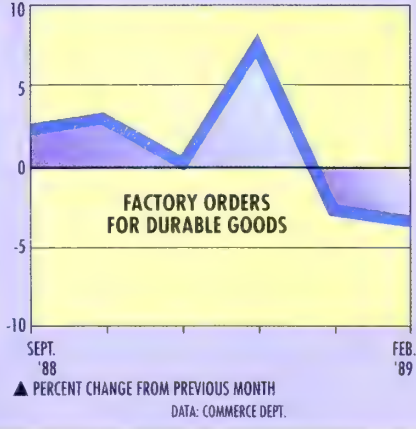
pressures grow, this balancing act will be increasingly hard to pull off. "Can you continue to grow at a reasonable pace and still contain inflation?" asks economic consultant William N. Griggs of Griggs & Santow. "It would be a neat trick." Adds Robert H. Chandross, chief North American economist at Lloyds Bank PLC in New York: "There's a very narrow glide path. If you miss by a fraction of an inch, you crash." **TAKING A BREATH.** If the Fed does pull it off, the slowdown could end up being nothing worse than a brief pause in the expansion. This much-hoped-for "soft landing" would take the steam out of inflation at the cost of few jobs and little disruption. "We can get through this with a rolling adjustment rather than a screeching halt," says Carol A. Stone, senior economist at Nomura Securities Inc. in New York. Not everyone thinks a soft landing is even desirable. Some economists worry that a modest slowdown would not do enough to break the back of inflation. The few jobs that would be lost would soon be restored, and, within a few months, the economy would be back where it started—facing the same old capacity and inflationary crunch. Says Alan Sinai, chief economist for Boston Co.: "This experiment of slow tightening to ease the economy down has never worked." More than that, these analysts believe that there comes a time when every expansion simply needs to take a breather. A recession now, they say, would give the Federal Reserve the flexibility to free the funds required to fuel a robust new expansion. A soft landing would force the central bank to keep one eye on inflation. That would leave little chance for a new burst of growth. "A recession gives the economy some running room for the future," says Morgan

THE ECONOMY IS SHOWING ALL THE SIGNS OF A SLOWDOWN

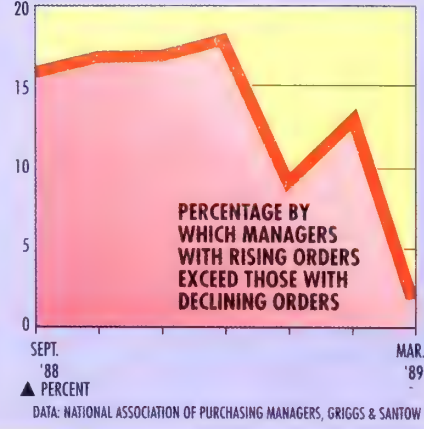
SHORT-TERM INTEREST RATES ARE UP...



...AND BIG-TICKET FACTORY ORDERS ARE DOWN...



...SO PURCHASING MANAGERS HAVE TURNED CAUTIOUS





McGrath: Adding GLQ223 to a tube of infected cells wiped out the virus in five days

FROM CHINA, A DRUG THAT TAKES AIM AT AIDS

GLQ223 appears to kill the virus—and shield healthy cells from harm

For months, San Francisco's tightly knit network of AIDS patients has been buzzing about a drug known as Compound Q. The rumors call it a Chinese wonder that cures AIDS in a single dose with no side effects. To those familiar with the cycle of hype and heartbreak that accompanies most new AIDS treatments, it sounded like another prescription for disappointment.

But an article in the Apr. 13 issue of *Proceedings of the National Academy of Sciences* does anything but debunk the mystery potion's promise. And while many AIDS researchers are too jaded to celebrate, it looks as if a remarkably potent new anti-AIDS drug, called GLQ223, may be on the horizon.

DUAL EFFECT. In laboratory tests at San Francisco General Hospital, GLQ223 revealed a startling property: When injected into a test tube of cells infected with the AIDS virus, GLQ223 not only eliminated all trace of the virus within five days but also protected other cells from infection. This dual effect is still not entirely understood, says Michael S. McGrath, the University of California at San Francisco researcher who conducted the tests and wrote the article. What is known is that GLQ223 works differently than other high-profile AIDS therapies. The substance contains an enzyme that cuts apart ribosomes in cells infected with HIV, the AIDS virus. Ribosomes

are like microscopic protein factories that keep a cell alive. McGrath says the assault on ribosomes seems to stop AIDS infection cold by killing cells before the infection can spread.

In contrast, Burroughs Wellcome's AZT interferes with the reproduction of HIV. CD4 therapy, an experimental treatment being tested by Genentech, SmithKline, Biogen, and others, floods the body with counterfeit agents that clog the virus' infection sites.

There's more to McGrath's findings than the drug, however. Much of the early AIDS research focused on T-lymphocytes, the body's infection-fighting white blood cells. T-cells were believed to be the virus' prime target, and protecting or rejuvenating them became the goal of many treatment projects.

But McGrath and others have long argued that another type of cell, the macrophage, deserved more attention. Macrophages course through the body gobbling viruses, bacteria, and other in-

Human testing is still to come, but Swiss giant Sandoz has already locked up worldwide marketing rights

vaders. About a year ago, researchers began finding HIV in macrophages. That was an alarming discovery, since macrophages, unlike T-cells, don't die when infected by HIV. Instead, they become circulating reservoirs of infection.

McGrath's article contains the startling finding that 2% to 7% of the circulating macrophages in an AIDS patient's blood may be HIV-infected—vs. just 1 in 10,000 T-cells. Most researchers previously assumed an upper limit of about 1%. "Macrophages may really be the primary target" of HIV, says Thomas M. Folks, who directs a virus laboratory for the Centers for Disease Control and also works with macrophages.

CUCUMBER SURPRISE. The notion of billions of macrophages serving as hosts for HIV led McGrath to trichosanthin. A visiting Chinese scholar told him more than two years ago that the substance, an extract of a protein found in a member of the cucumber family, seemed unusually good at killing macrophages. McGrath later found that in small doses it also killed infected macrophages and left others alone.

Much work still needs to be done, particularly the clinical trials that could turn GLQ223 into a real drug. Trichosanthin has been used in China for years to induce abortions and more recently to treat certain cancers, with few reported side effects. However, it took Genelabs Inc., a little-known, privately held Redwood City (Calif.) biotechnology company, to come up with the ultrapure form, GLQ223, used by McGrath. Genelabs hopes to win approval soon from the Food & Drug Administration to begin trials of GLQ223, which has never been used on humans, at San Francisco General's pioneering AIDS clinic. Swiss drug giant Sandoz Ltd. has locked up worldwide marketing rights.

The trick now may be controlling its use. BUSINESS WEEK has learned that tiny Alpex Inc. in Oakland, Calif., already plans to make a "Compound Q" of unknown origins available to AIDS patients by May 1. The one-man company's president, Fred Ponder, who is himself HIV-positive, defends his right to speed access to the drug: "We can't wait the years and years it takes to get a drug through testing."

That attitude worries Genelabs President Frank Kung. "GLQ223 is a drug prepared in the classical sense," he says. "We don't know what's in the crude extracts." In the wrong hands, adds McGrath, trichosanthin can be highly toxic, "even lethal. The last thing we need is people running off to China for magical white powders. That's why we've practically been testing this thing in secret." The secret is out now, but the most important testing is still to come.

By Joan O'C. Hamilton in San Francisco

HP: NOW NO. 1 IN WORKSTATIONS

The deal for Apollo is a giant step, but keeping that lead may be hard

It's no secret to computer industry insiders that Apollo Computer Inc. has been quietly shopped around in the past year. The company that pioneered the engineering workstation—now the hottest segment of the computer market—had slipped further and further behind market leader Sun Microsystems Inc., and its anemic stock price made it the subject of constant takeover rumors.

The surprise came on Apr. 12 when Hewlett-Packard Co. emerged as the buyer. In an uncharacteristic move, the staid HP agreed to pay \$476 million for Apollo, which had sales of \$654 million last year. "There aren't many deals with this good of a fit," says HP President John H. Young. Sun President Scott McNealy takes a different view: "I believe Apollo thought it couldn't make it alone, and HP felt it couldn't catch up."

BIG LEAP. Indeed, the marriage of No. 3 HP and No. 4 Apollo catapults the duo beyond Digital Equipment Corp. and just slightly ahead of No. 1 Sun, which has about 28% of the workstation market, according to market researcher Dataquest Inc. That's an impressive leap for HP, which was barely a factor two years ago. Even with a respectable 17% market share, HP has had to hustle to get software companies to write pack-



HP'S YOUNG PAID \$476 MILLION FOR APOLLO

ages for its workstations. For that reason "HP desperately needed to be No. 1 or No. 2," says analyst Vicki J. Brown of International Data Corp.

HP's challenge will be keeping the 30% market share it now has on paper. Digital and Sun recently have made aggressive product moves (page 139), and IBM is expected to do the same later this year. At minimum, however, the deal should help Apollo hold on to its customers. "Apollo has been doing well technically," says James W. McGean, who buys Apollo products for McDonnell Douglas Corp. "Their big problem has been lackluster business performance."

Customers have grown increasingly jittery over Apollo's shaky financial results under Chief Executive Thomas A. Vandersla, who will take home \$7.2 million for his 1.5% of the company.

The acquisition does pose marketing problems. Although Apollo's strength in computer-aided software development and publishing shores up HP weakness, the two companies overlap in electronics design and engineering. And one of Apollo's biggest resellers, Mentor Graphics Corp., is a head-on competitor with HP in computer-aided design.

SAD FINALE. A lot will depend on how well HP combines its product lines with Apollo's. The easy part will be merging the two companies' lines that use the same Motorola Inc. microchips. But both Apollo and HP use proprietary chip designs for their high-end machines. The two companies have spent years developing

these RISC (reduced instruction-set computing) processors. Apollo's most powerful RISC computer, a four-processor behemoth, has four times the speed of HP's top-end Spectrum model. Nevertheless, after a five-year effort to develop Spectrum, HP is unlikely to give it up.

Eventually HP is expected to phase out Apollo's RISC design but adopt its multiprocessor approach. That would mark a sad finale to Apollo's tale. For two years, RISC has been the key to Apollo's revival efforts. A fast-moving market just didn't give it the luxury of time.

By Jonathan B. Levine in San Francisco with Leslie Helm in Boston

CONTROL DATA MAY FINALLY HAVE THE RIGHT STUFF

Control Data Corp., ailing giant of the computer biz, is trying to fix itself—again. Observers are cynical: CDC promised it would bounce back many times in the past few years.

But any day now, CDC's new president and chief operating officer, Lawrence Perlman, will unveil his plan. And Wall Street analysts are cautiously optimistic that he can halt CDC's slide—which Chief Executive Officer Robert M. Price hasn't done. Perlman already put CDC's Commercial Credit Corp. unit into good enough shape to be sold for \$843 million. Then he turned the disk-drive unit from a low-quality laggard into one of the best in the business. "Perlman is the only CDC executive with a remote chance of suc-

ceeding," says one analyst. "Finally, they have somebody at the wheel who has a license to drive."

Analysts say that a trimming of Control Data's mainframe business, including a blizzard of pink slips, is a certainty. The slow-growing unit last year lost \$35 million. Perlman's record at Imprimis, the disk division, offers a clue: By asset sales and layoffs, he halved the payroll to 9,000 in two years.

JOINT VENTURE? His biggest headache is the ETA supercomputer subsidiary. Once regarded as CDC's best chance for a comeback in scientific computing, ETA Systems Inc. has lost \$238 million since 1985 and \$100 million last year alone. The software for its highest-margin machines still doesn't work

well. That has dried up sales. Perlman's solution may go beyond layoff. Rumors abound that he'll seek a joint venture partner, perhaps a Japanese supplier such as Fujitsu, to help shoulder the ETA burden. "It's not written in stone that Control Data has to own 100% of ETA or 100% of its [mainframe computer operations]," notes Perlman.

Lacking a fix for CDC's computer businesses, the company may relieve its cash crunch and appease bankers by selling off profitable units such as Arbitron, Imprimis, or Ticketron. That would be like breaking up the furniture to feed the fire, but there may be little choice. Once-proud CDC is bound to keep shrinking.

By Russ Mitchell in Bloomington, Minn.

GULF & WESTERN IS READY TO GO OFF ITS DIET

slim—and looking for media or entertainment companies to gobble

Gulf & Western Inc.'s Paramount Pictures made lots of money in sequels of such as *Star Trek* and *Raiders of the Lost Ark*. Now it's CEO Martin S. Davis' turn to produce a corporate sequel of his own. On March 9, Davis announced he'll soon end a six-year divestment spree. G&W is ready to stop buying again, but its latest plot has a twist: Eschewing conglomeration, G&W will be plunging deeper into media and entertainment game.

Davis plans one more sale: he could raise more than \$3 billion by selling The Associates, G&W's financial-services arm. It contributed 40% of Gulf Western's \$5.1 billion in revenues for last fiscal year, ended October, and cut half its \$748 million in operating expense. Once it's gone, G&W will become amount Communications Inc.

Davis says he already has his eye on the properties. And while he doesn't shun hostile bids, he says: "Think of me as more than unfriendly, and don't count joint ventures, foreign partnerships, or investments in other companies." He calls the speculation that G&W might go private "dead wrong."

Analysts and investors wasted little time trying to imagine where Davis might strike. The top candidates include Tribune. The Chicago-based newspaper and broadcasting company is a favorite because of its TV stations and programming. With the six independent outlets June Co. owns in such major cities as New York, Los Angeles, and Chicago, Davis could build a TV network. That would give him a home for Paramount's shows and Tribune's syndicated fare such as *Geraldo* and *At The Movies*. Even the Chicago Cubs, Tribune adds a popular team to the sports G&W airs on cable with its New York Knicks and New York Rangers franchises.

If G&W moved in, the company might be able to sell the *Chicago Tribune* and



G&W's DAVIS: IS HE EYEING TRIBUNE, MCGRAW-HILL, AND MCA?

New York *Daily News*. The Federal Communications Commission prohibits cross-ownership of newspapers and TV stations in a community. Tribune has no problem now: The FCC gave exemptions to companies that owned both properties when the rule was established.

A deal with Tribune could run more than \$4.5 billion, and it would probably have to be friendly, since Tribune has adopted several defenses, including an employee stock ownership plan. But G&W is on good terms: Paramount distributes some of Tribune's TV shows.

■ **McGraw-Hill.** Davis has long been interested in the company, which owns *BUSINESS WEEK*. There's an obvious fit in publishing: G&W's Simon & Schuster Inc. and McGraw-Hill Inc. are both leaders in educational publishing. McGraw-Hill's Standard & Poor's Financial & Economic Information Co. would help G&W build its professional information services. McGraw-Hill also owns four TV stations.

Some analysts consider McGraw-Hill vulnerable, especially to a premium-price cash offer. But insiders control about 20% of the stock, and the company would likely mount a tough fight, as it did against American Express in 1979. The question is: Does Davis want to spend about \$5 billion to expand in publishing when G&W's most exciting opportunities seem to be in entertainment?

■ **MCA.** Davis knows MCA Inc. well. They compete in film and TV production, movie theaters, and book publishing. They're partners in a foreign film-distribution company, an international videocassette distribution operation, and cable's USA Network. Davis also might like MCA's theme parks and record business.

But obstacles could be insurmountable even if G&W is willing to pay more than \$5 billion for MCA. The Justice Dept. might object to a merger between major studios. And G&W would have trouble striking a friendly deal with a company where executives, including President Sidney Sheinberg, like their jobs.

■ **Capital Cities/ABC and CBS.** Virtually every producer would love to own a TV network. Problem is, the government prohibits the Big Three from syndicating the programs they air. The networks are desperately trying to change that restriction. Until that happens, G&W would be taking a huge gamble by investing in either Capital Cities/ABC Inc. or CBS Inc.

■ **Other contenders.** In film, there's speculation over Columbia Pictures Entertainment Inc., which is controlled by Coca-Cola Co. and whose stock lately has been hitting new highs. For publishing and information, Davis could try Dun & Bradstreet Corp. or Houghton Mifflin Co. Some investors are hoping G&W will offer more for Time Inc. than they'd get from a merger with Warner Communications Inc. And if Davis wanted to pull off a stunner, he might listen to Dennis McAlpine, an Oppenheimer & Co. analyst: He wonders whether General Electric Co. would trade NBC Inc. for The Associates, which would add muscle to GE's huge financial-services arm.

Davis may have his next move already planned. But, as with most sequels, all he'll say is... to be continued.

By David Lieberman in New York, with James E. Ellis in Chicago and Ronald Grover in Los Angeles

EXECUTIVE SUITE

LAST CHANCE FOR LOVE?

National Intergroup's board tells its CEO to get results—or else

Through four straight annual losses at National Intergroup Inc., Chief Executive Howard M. Love has depended on a loyal board of directors for his survival. But Love's latest victory—quashing a coup attempt by President Laurence J. Farley—has been costly. The board has put Love on notice that he needs fast results to save his job.

In a terse announcement on Apr. 6,

NII said that Farley was resigning "due to irreconcilable differences concerning senior management responsibilities." James S. Pasman Jr., former CEO of aluminum maker KaiserTech Ltd., will replace him. Farley's departure shocked many of NII's major bankers and investors, who felt that he was a key to NII's turnaround. "Love hasn't shown he can do the job," says Richard P. Petran, a portfolio analyst at the Wisconsin State Investment Board, one of NII's biggest shareholders. "We needed a change, and that was obvious to the board." Love, Farley, and most of NII's directors declined to comment for this article.

BITTER BATTLE. Three sources close to the board say that Love is working against a tight deadline. Already under pressure from an investor group led by raider Charles Hurwitz that has bought up 8% of NII's stock, the company will soon announce results for the year ending Mar. 31. Most analysts expect another loss. Love, says one board source, "had better make NII perform in the next fiscal year, or the board will have to make a hard decision."

Farley's resignation capped a bitter three-week boardroom battle. Since Farley came on board in February, 1988, Love had relinquished most of his responsibility to the former chief executive of Black & Decker Corp. Farley had made aggressive moves to bolster NII's finances and begun to fix the company's core drug distribution business.

In mid-March, Farley launched his revolt. Sources say Farley told outside directors that Love wasn't moving fast enough to fix NII, including selling off the company's ailing Ben Franklin retail chain. Farley proposed that he—or an outsider of the board's choosing—become chief executive. Love would be left with the largely ceremonial chairman's slot.

The battle peaked at a tense, four-hour board meeting with NII's outside directors at the company's Pittsburgh headquarters on Mar. 21, where both men argued their cases. By early April, the board had decided that Farley had overplayed his hand and had to go. To replace him, the directors hired Pasman, whom they were already considering for the chief financial officer's position.

Now all Pasman has to do is help rescue NII—and Love's job. But can he move fast enough? Executives at mutual fund giant FMR Corp., who are considered some of Love's biggest supporters, are losing patience. Says Stephen Hurley, an FMR portfolio manager: "This is the year that NII has to start delivering." Time is running out for Howard Love.

By Gregory L. Miles in Pittsburgh

PEOPLE

PUTTIN' ON THE RITZ—IN NEW YORK, WASHINGTON, ASPEN...

Mohamed Hadid makes some flashy hotel deals—but will they pay off?



THE RITZ IN HIS MITTS: HADID IS SPENDING BIG TO RESTORE THE HOTEL'S CACHET

He buys and sells real estate with the abandon of a Monopoly player, loves acquiring elegant hotels, mixes with the rich and powerful, and dreams of owning an airline. Donald Trump? Guess again. Meet Mohamed Hadid, a dapper Washington developer who has begun to attract national attention with a flurry of high-powered deals.

On Apr. 6, Hadid made Manhattan's real estate moguls take notice when he engineered the \$141 million acquisition of the Ritz-Carlton hotels in New York and Washington. That signals that Hadid, who already is building other Ritz-Carltons in Aspen, Colo., Scottsdale, Ariz., and Houston, intends to be a power in luxury hotels. And with \$300 million in office projects under way in Washington, he's already a force in the capital's clubby real estate circles.

A Palestinian emigré, Hadid, 40, arrived in the U.S. in the 1960s. After cutting a wide swath through Washington real estate in the early 1980s, he now plans to go international. He speaks

boldly of building more Ritz-Carltons in Europe and Asia. He even muses that like Trump, he may one day see his name on a plane. "I would love to be on an airline," says Hadid, who pilots a twin-engine Piper Navajo to his estate on Maryland's Eastern Shore.

But while Hadid clearly has the ambition and the trappings of a Trump or Helmsley, it's not yet clear that he has their resources. The Rosslyn (Va.)-based developer claims a net worth of roughly \$90 million, much of it equity in Washington office buildings, and he's backed by Japanese banks and Middle Eastern investors. Industrial Bank of Japan Ltd., for example, committed \$70 million in loans to the Aspen Ritz. Another Hadid backer is the Saar Foundation, a Virginia-based group that is a 50-50 partner in Hadid Holdings.

In a typical deal, Hadid puts in a small amount of equity, takes on a partner to buy the land, and then finances the development through a commercial bank. In the recent Ritz deals, Hadid is committing only \$20 million in letters of credit secured with personal certificates of deposit, according to his lawyer.

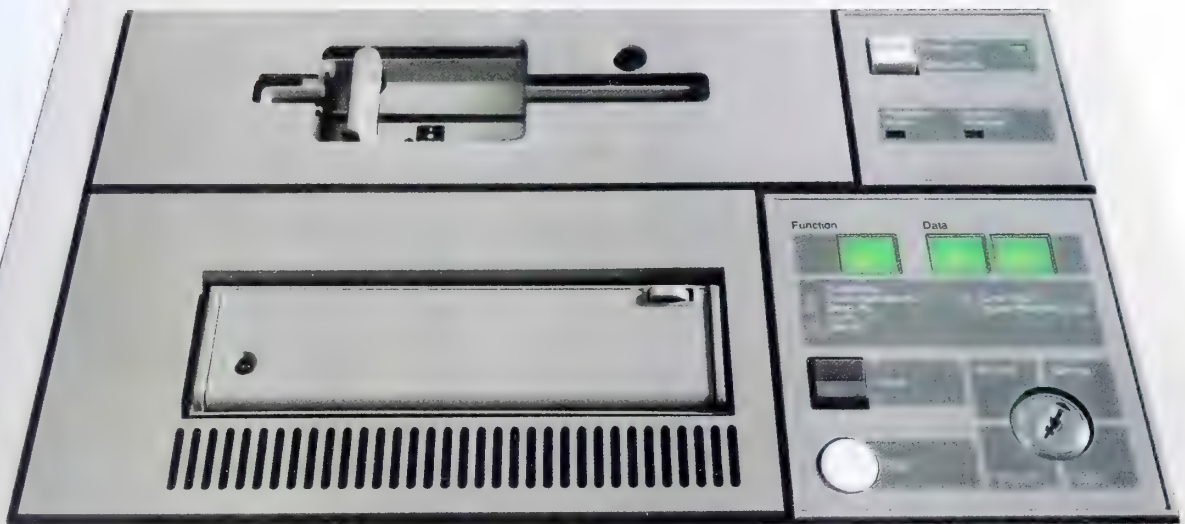
RITZ RUTS. Local developers appear to consider him a good risk. Martin K. Lloyd, president of Stanley Martin Cos., a major Virginia developer with whom Hadid is building houses, praises his partner as "a genuine individual with a great marketing flair."

Not everyone's experience has been pleasant. American Security Bank has gone to court to get back a \$500,000 personal loan it extended to Hadid. In 1987, Dominion Federal Savings & Loan Association last year successfully sued Hadid to cure repayment of a \$13.5 million loan.

Perhaps the biggest question about Hadid is whether his foray into the hotel business will pay off. In recent years, some Ritz-Carltons have fallen on hard times, and the name may have lost some of its former cachet. Meantime, rich people have rushed into the luxury market, building major cities with scores of expensive hostleries (page 111).

Few doubt Hadid's eagerness to get a deal, however. Just ask Trump. In 1987, Hadid snared a valuable piece of Aspen real estate out from under Trump's nose. The deal was vintage Hadid. A Texas developer had plans to build a hotel but ran out of

**“What my little company needs
is the kind of computer only
a big company can afford.”**



money. Two Texas thrifts and a handful of other creditors stood ready to foreclose. Trump reached agreement with one of the thrifts to buy a portion of the land after foreclosure for \$17 million. But Hadid's lawyers went to the developer, the second thrift, and the other creditors and cut a \$42 million deal to buy the entire package.

OUT-TRUMPED. Trump is suing Hadid and the thrift he dealt with, but construction has begun on the 292-room Ritz-Carlton at the base of the ski slopes. The suit is pending in Denver federal court. Trump says only that Hadid is "a man who believes in paying unlimited amounts of money for anything."

In the New York and Washington deals, Hadid is again capitalizing on the

misfortunes of another developer. He is paying \$141 million to retire debts run up by John B. Coleman, who bought the hotels in 1982 and filed for bankruptcy in 1986. Hadid vows that after a \$50 million redo, his property on Central Park South "will be the best hotel in New York."

With his white Rolls-Royce convertible and his elegantly tailored suits, Hadid has all the trappings of a successful developer. But appearances can only carry him so far. To really make his mark, Hadid will have to prove he is as skilled at owning hotels as he has been at buying and selling office buildings.

By Tim Smart in Rosslyn, Va., with Sandra D. Atchison in Denver and Harris Collingwood in New York

glossy pictures and voluminous footnotes—were rumored to be the net rage. Yet the number of summary formats so far this year is actually below the 1.5% of 11,000 reports issued in 1987, according to Sid Cato, publisher of a newsletter on annual reports.

RAGING SURF. Broad themes were back this year, skyrocketing to 45% of reports issued from 26% last year, Cato says. The cover of GTE Corp.'s annual, for instance, is emblazoned with a stark lightning flash and the words "The Power Inside, poetic excerpts pertaining to "power" accompany photos of GTE executives in settings worthy of Emily Brontë's *Wuthering Heights*. One GTE manager is seen straddling mossy rocks whipped by a raging surf.

Bartlett's was well-thumbed: At least a dozen reports feature literary quotes on the cover or inside, including the ever-popular Charles Dickens quotation, "It was the best of times, it was the worst of times..." Harsco Corp. resorted to the line this year—mainly to brace investors for the worst.

Sensitive, "people-oriented" annuaries are more popular than ever. Look for covers such as TRW Inc.'s "15 who make a difference" or First Pennsylvania Corp.'s report full of two-page testimonials lauding employees. General Motors Corp. made its cars the heroes of its report, with a half-dozen photo spreads that look like ads in swanky magazine.

FLYING WHALE. For just plain fun, try Southwest Airlines Co.'s report, which trades on the carrier's status as official airline of Sea World in San Antonio, home of Shamu, the killer whale. The carrier offers a colorful paper airplane cutout: "Here's your very own Shamu. One, compliments of Southwest Airlines. You, too, can teach a whale how to fly."

As usual, a number of companies try a mix of *glasnost* and spin control. General Electric Co. Chairman John F. Welch Jr. confesses in his letter to shareholders that a new GE rotary compressor is a "problem" that will represent a "substantial" cost to GE. But try locating that cost. Although the problem is tread-

ed indirectly in various places, not until the report's last page does it say that the net impact of the "problem" is \$297 million—add to get that figure, investors must do some addition.

As for Goldome, it maintains that its newspaper format wasn't a direct ripoff. After all, says Chodorow: "I don't think you generally see a headline across the top of *USA Today* as negative as the one we chose." It read: "Goldome posts loss, writes down real estate."

By Andrea Rothman in New York, with bureau reports

ANNUAL REPORTS

'HELLO, SWEETHEART, GET ME CORPORATE PUBLIC RELATIONS'

1988's annual reports include a newspaper look-alike and a paper plane

Goldome, a Buffalo-based savings bank and financial-services company, decided to have a little fun with its annual report this year. Eschewing the traditional format, it produced a report that bears a striking resemblance to *USA Today*. The report includes a "Goldome Sports" section (read about company bowlathons), "Goldome Living" (featuring a trombone-playing vice-president), and "Goldome Business." The idea, says the report's editor, Marc Chodorow, was to make it more readable and draw a little attention to the bank.

It attracted attention all right. Law-

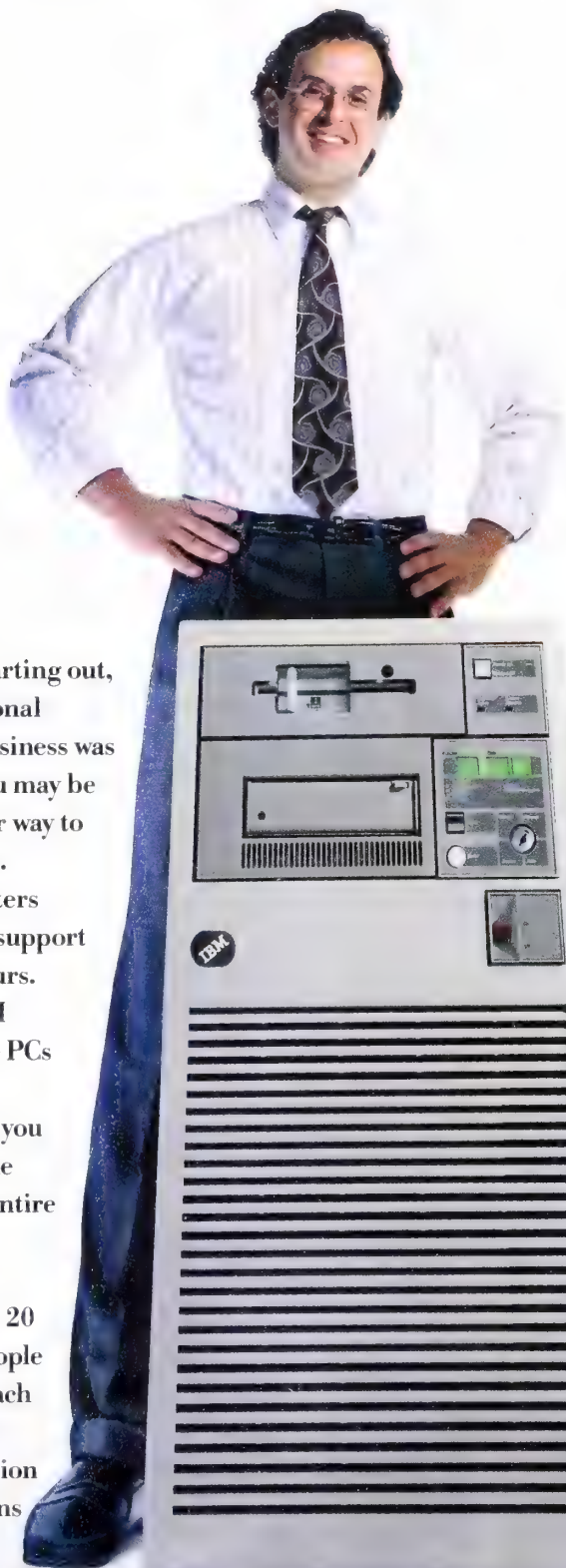
yers for Gannett Co., publisher of *USA Today*, sent a stern letter to Goldome demanding that it contact all 45,000 shareholders and "publicly apologize for the unauthorized appropriation" of the newspaper's format. According to Chodorow, Goldome and Gannett lawyers are now negotiating.

Such controversy is the last thing most companies want at annual report time. That might explain why one supposedly up-and-coming trend seems to have fizzled: Last year summary reports—the no-frills annuals that dis-

GOLDOME'S KNOCKOFF OF USA TODAY DID NOT AMUSE GANNETT, WHICH DEMANDED A PUBLIC APOLOGY



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SALINAS SCORES A COUP WITH THE IMF

► Mexico won the race to be the first debtor nation to benefit from Treasury Secretary Nicholas Brady's new debt strategy, signing an agreement on Apr. 11 for a three-year, \$3.64 billion loan from the International Monetary Fund. A substantial part of the loan will finance deals to reduce Mexico's \$70 billion in debt to foreign banks—the main feature of Brady's plan.

The IMF loan is a coup for Mexico's new president, Carlos Salinas de Gortari, and the market-oriented reforms he's pushing. It's likely to be followed soon by a \$1.5 billion loan package from the World Bank. But official lending is only the first step: To return Mexico to growth, Salinas still needs a surge of private investment and a deal with the banks to cut Mexico's annual debt service. Talks with the banks, expected to begin on Apr. 19, will be "arduous and difficult," says Finance Secretary Pedro Aspe.

A DRUGMAKER SAYS 'YES' TO CRAY

► Cray Research, the supercomputer maker, has found its first pharmaceutical industry customer in Eli Lilly. The drugmaker will use its new \$12 million Cray-2 machine to model in minutes experiments that otherwise might take weeks in a test tube. The sale is key to Cray's commercial push beyond auto, aerospace, and oil companies and into the pharmaceutical and chemical industries, where it seeks new growth.

THE FEDS COLLAR A CALIFORNIA BIGWIG

► A San Francisco businessman who allegedly tried his hand at drug dealing and money laundering was taken to the cleaners in a

Richard Silberman, who struck it rich in the 1960s as a partner in the Jack-in-the-Box fast-food chain and later served as California's finance director under former Governor Jerry Brown, was arrested on Apr. 7 on federal money-laundering charges.

The government charges that Silberman, 59, offered to help alleged mobster Chris Petti launder dirty cash and was directed to a man Petti thought was working for Colombian cocaine traffickers. Petti's contact was in fact an undercover FBI agent. Silberman had laundered \$300,000 and was negotiating for \$1.1 million more when the trap snapped shut, the government alleges. Silberman could not be reached for comment.

SMITHKLINE AND BEECHAM ARE ENGAGED

► SmithKline agreed to team up with Britain's Beecham Group to form a \$6.7 billion drug industry giant. The deal calls for SmithKline chief Henry Wendt to chair a merged board, while Beecham's Robert Bauman would serve as CEO. Admits Wendt: "It would have been more fun for me if I was the CEO."

U.S. and British shareholders each get half the new company, with a cash dividend soothing SmithKline holders. After SmithKline shed its nondrug units, the new company would focus on drugs, over-the-counter medi-

YOU SAW A COW WHERE? SHUT UP AND DRIV

Cattle rustling, even in this day and age, isn't unknown in western Wisconsin. But farmers thought it a bit strange when, last December, their calves and yearlings began disappearing one by one. Especially puzzling were the tire tracks that sometimes were found leading into the barnyard. "It was a real narrow vehicle," farmer Dan Golden told the *Minneapolis Star-Tribune*. St. Croix County Sheriff Ralph Bader admits he was baffled. "A lot of cattle thieves use trailers," he says.

The case apparently was solved when secret informants and sheriff's deputies to arrest two suspects. Seems the case some weighing 650 pounds, had been stuffed into a getaway car through its rear hatch. "It couldn't have been easy getting them in," says Sheriff Bader. "And it would have been pretty snug in there." The miscreants' vehicle: a subcompact Chevrolet.



cines such as Tums, and animal medicines. Barring a challenge, the deal could be wrapped up by August.

THE DIFFERING FATES OF TWO MOVIE MOGULS

► Foreign moguls continue to buy up Hollywood. Australian Christopher Skase, 40, will pay Kirk Kerkorian \$600 million for United Artists. The onetime financial writer owns the top TV network in Australia and luxury hotels there and in Hawaii.

Skase intends to make the film and television studio a major supplier for his network and other markets, focusing on Japanese invest-

ments as partners. He says.

Meanwhile, Italian financier Giancarlo Parretti's rush to buy into Hollywood has been slowed. New World Entertainment, which had agreed in February to be purchased by Parretti, will instead go to Revlon Chairman Ronald Perleman for about \$145 million. Parretti, who has been looking to snap up struggling independent studios, earlier bought Cannon Group.

AN INSIDE TRADER IS SENTENCED

► William Dillon, the former Merrill Lynch stockbroker who made about \$118,000 in trading profits by using information from illegally obtained advance copies of *BUSINESS WEEK*, was sentenced on Apr. 11 to two years in prison, three years of probation, and 200 hours of community service. U.S. District Judge John Walker suspended 18 months of the prison term.

Dillon, who until last July worked in Merrill Lynch's New London (Conn.) office, pleaded guilty last year to a count of wire fraud. He obtained his inside information by buying copies of *BUSINESS WEEK* from employees of nearby printing plants.





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High stakes for America:

We're not investing. On key indicators like fixed investment and civilian R&D expenditures, Japan has doubled its lead over the U.S. since 1979. During this decade of merger mania, Japan's manufacturing productivity rose 60%; faster than ours.

We're "debt poor." Around 25% of corporate cash flow now goes for debt service, including billions borrowed to pay for takeover games. That's money competitors in Japan and Europe can use for research and new product development.

Our technology's slipping. Foreign inventors were issued 47% of all U.S. patents last year—one-fifth of the total went to the Japanese alone.

We're exporting our strength. While the competition has been building technological and worker strength in their own nations, American corporations have hiked offshore investment by 50% since 1983—U.S.-based multinationals now do over 25% of their manufacturing outside the U.S.

There's greed at the top. American CEOs make up to six times what CEOs earn in 14 other industrial nations. Compensation for top U.S. executives shot up 51% in the last five years and bears no relation to company performance.

It's time to turn it around.

American business should put America's future first.



International Union, UAW

THE SKELETONS IN JIM WRIGHT'S CLOSET KEEP RATTLING CONGRESS

Say what you want about House Speaker Jim Wright (D-Tex.), his full-throttle approach to legislating made the last Congress one of the most productive in years. But as the House ethics committee considers bringing misconduct charges against Wright—charges that would throw the House into turmoil and might ultimately cost the Speaker his job—a siege mentality is settling in on Capitol Hill. Whatever the ultimate applies to the first session of the 101st Congress, it won't read "can-do."

With Wright digging in for a long fight, Democrats' ability to use the House to stage assaults on the Bush Administration will be severely impaired. And the longer Wright's agonies last, the more Republicans on the Hill will like it. "There's plenty of time between now and 1990 to chew the final ethics report," says new House majority Whip Newt Gingrich (R-Ga.), Wright's chief tormentor.

E BOASTS. For his part, the Speaker is talking business as usual. He boasts that in coming weeks the House will pass a clean-air bill, \$2.5 billion in federal aid for day-care centers, legislation requiring employers to provide parental leave, campaign finance reform, nonmilitary aid to the Nicaraguan *contras*, and new restrictions on television programming for children.

But in the cloakrooms, Democrats are already murmuring about signs that the Speaker's declining influence is jeopardizing his goals. After vowing early on, he was unable to muster enough support for a pet bill that would require foreign investors to register with the Commerce Dept. His solution to the strike at Eastern Air Lines—legislation setting up an emergency board to recommend settlement—stalled and ultimately was overtaken by events (see p. 24). And in pushing through a minimum-wage increase, Wright sent the wrong signal to the White House. He fell 28 votes short of the two-thirds majority he will need to override almost certain veto from President Bush.

Despite Wright's bravado, his first priority is survival. His

aides breathed a sigh of relief when the ethics committee agreed secretly on Apr. 5 to drop charges that Wright improperly pressured federal regulators to go easy on failing Texas savings and loans. They think Wright can weather charges that he skirted limits on honoraria by selling copies of his memoirs to groups in lieu of speaking fees. "So a few zealous Wright staffers suggested something that was in bad judgment," says one of the Speaker's strategists. "Big deal."

But Wright could be skewered on charges that his partnership with Texas developer George Mallick—who feared S&L regulators would force foreclosure of loans he cosigned—gave unreported gifts to the Speaker and his wife.

Whatever charges the committee files, Wright is in for a long ordeal. Ethics panel rules give him 21 days to respond. Then the committee would move to hold a disciplinary hearing, and Wright would have additional time to respond. A final resolution—which could range from censure to a slap on the wrist for "technical violations" of House rules—probably won't go to the floor until this summer. Meanwhile, the media will have a field day with Special Counsel Richard J. Phelan's documenting of Wright's financial affairs.

SHOWING NO MERCY? Democrats aren't eager to leap to Wright's defense. Many blame him for the loss of a 51% pay raise. And Senate Democrats' rejection of John G. Tower as Defense Secretary leaves their House colleagues worried about charges of hypocrisy. Some fear that the Wright mess could hurt them at the polls in 1990. "Democrats," says University of Virginia political scientist Larry J. Sabato, "aren't in a mood to be merciful."

Still, it is by no means clear that the Bush White House will profit greatly from the Democrats' distress. A paralyzed House may also block what few legislative initiatives the Administration has mustered. And the partisan rancor fueled by the Wright affair may linger, making a mockery of Bush's hopes for a new spirit of bipartisan cooperation.

By Douglas Harbrecht



HOUSE SPEAKER WRIGHT

PITAL WRAPUP

ECONOMICS

Joint Economic Committee Chairman Lee H. Hamilton's (D-Ind.) effort to build the panel's prestige is bearing fruit. For the first time since 1980, the committee will issue a consensus report on the state of the economy. Democrats accepted the conclusion that the economy has grown strongly throughout the 1980s and "is not about to fall off a cliff." Republicans conceded that the U.S. still faces problems of poverty, homelessness, and competitiveness. During the Reagan years the committee often produced Democratic and Republican reports so different that the reader was left wondering if they were

looking at the same economy. Representative Hamilton and Delaware Senator William V. Roth Jr., ranking GOP member, hope that more realism will restore to the panel its 1970's clout.

DEFENSE

Defense Secretary Richard B. Cheney is doing some grunt work. With the Pentagon expected to propose \$16 billion worth of spending cuts to Congress by Apr. 24, Cheney has taken personal charge of the budget effort—a job usually left to the Deputy Secretary. According to Pentagon scuttlebutt, Cheney may call for early retirement of some aircraft carriers and putting other ships into the reserve.

THE CAPITOL

Loews Hotels Inc. Chairman Preston R. Tisch is headed for a new assignment in Washington. The former Postmaster General will soon be named co-chairman of the new U.S. Capitol Preservation Commission. Tisch and fellow members Senator Robert C. Byrd (D-W.Va.) and Representative Lindy Boggs (D-La.) are charged with raising funds to acquire and preserve historic furnishings, paintings, and manuscripts associated with the building. Congress created the panel last year to hit up the private sector for the money to "ensure proper preservation of this national treasure."

"Management must guide the forces of change..."

— John W. Teets, Chairman



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Hard choices were faced; tough decisions were made. Subsidiaries with annual sales of \$3 billion,

including the company's nationwide bus line, were divested. At the same time, new businesses with excellent growth and profit potential were established or acquired.

For example, Purex household and laundry products were added to the personal care and packaged foods brands of Greyhound's Dial Corporation. Premier Cruise Lines, the official cruise line of Walt Disney World, was launched. Dobbs food service for air



elers was acquired, complementing Greyhound's
ing airport and food service businesses. General
ors' RTS transit bus manufacturing and parts opera-
was purchased to expand Greyhound's top-ranked
city coach-building business.

Today, Greyhound's four business segments —
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g and financial — produce revenues at a \$3 billion
ual rate.

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further improvement of operating returns. Change is
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of change to create value for shareholders.

At Greyhound, we believe in renewing the com-
pany day by day.

The Greyhound Corporation



THE EUROPEANS' BIG PROBLEM: WHAT TO DO WITH ALL THAT CASH

They're celebrating in Europe's boardrooms. With economic growth running at its swiftest pace in 12 years, corporations are reporting blockbuster profit gains for 1988. On average, estimates analyst Angus McNeillage of British broker James Capel & Co., earnings were up about 16%, with many companies showing even bigger gains. This year is also shaping up as a good one, although it may not be another record-breaker. And chances of a slowdown in the U.S. economy are growing (page 21), posing a threat to Europe's export-oriented companies.

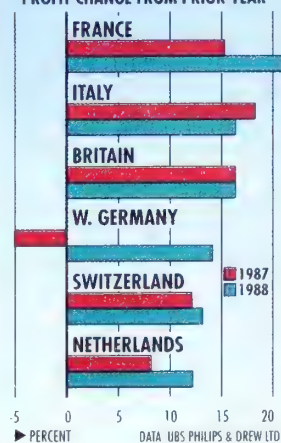
For now, though, the profit boom is creating new jobs for Europeans and better returns for investors worldwide. Many manufacturers, their plants running full tilt, are fattening capital spending plans. Dividends are going up. And with the cheap dollar and the barrier-free European Community of 1992 posing buying opportunities, many cash-rich companies are stepping up their acquisition activity at home and in the U. S.

reason why German companies are able to salt more away for mergers and expansion: "Profits are growing at twice the rate of wages," says Hubert Günter, head of research at Bank in Liechtenstein's Frankfurt branch.

The lofty profit growth (chart) is spread across the business spectrum. Capital-goods makers are benefiting from Europe's investment boom. So are chemical makers. And robust consumer spending and the industrial revival are giving auto makers a boost. Dutch truck maker DAF, for one, saw earnings up 133% last year. Now, Chairman Aart van der Padt plans a "substantial" capital investment program for 1989.

jump. Passing on some of the extra profits, the French oil giant hiked its dividend by a third. After slimming down several lackluster units, German chemical maker BASF increased its earnings an estimated 44%. And Britain's Imperial Chemical Industries PLC turned in a 7% profit gain, to \$2.6 billion. ICI raised its dividend by 22% and will increase capital spending by up to 25%. It's also multiplying its investment in research and development, a huge expansion.

Apr. 28, ICI will sharehold- ers to ap- pro- a 57% hike in its rowing limit, to \$20 lion, in preparation a major product buildup or megamer- France's Rhône-P- lenc is equally ar- tious. Ranked No. 9 the world by sales, chemical maker w- to grow by acquisi- particularly in the U Over the past few y- it has purchased u- of Union Carbide C- and Stauffer Chem- Co. Now, with 3 year's earnings up 2% it is on the prowl



re. "We want to be among the top
e chemical companies in the world,"
7s Chairman Jean-René Fourtou.

Elf, meanwhile, is pumping up its
chemical division by buying Pennwalt
Corp., a Philadelphia maker of specialty
chemicals, for \$1.05 billion. And Swe-
r's Nobel Industries, its earnings up
% last year, already has poured \$117
million into EC acquisitions since Janu-
ry. More are planned.

Diversified industrial equipment mak-
ers are also humming. Dusseldorf-based
Thyssen saw profits soar 152%, to \$361
million, its best gain since 1953. The pay-
off: A 50% dividend hike and hints that
further increase might be in the offing
in 1989. Thyssen also is shopping for
acquisitions, mainly in Europe, in spe-
cialty steel, trading, and services.

THE NEXT YEAR? Despite warnings
from analysts about an impending slump,
many auto executives also are confident
for 1989. Cesare Romiti, managing di-
rector of Italy's Fiat, expects 1989's op-
erating profits will be "at least as good"
as those for 1988, when the auto, de-
fense, and aviation conglomerate turned
in a 23% gain, to \$2.8 billion. And despite
a sharp drop in exports to the U.S.,
Volvo's Volvo is rolling ahead with ex-
pansion plans. In recent months it has
launched a bid for a small Swedish in-
dustrial conglomerate, set up a real es-
tate venture, and drafted a plan to shift
its auto-making capacity to the Euro-
pean Community. Volvo would make the
move if the EC limits nonmember Swe-
den's access to the new unified market
in 1992.

Despite the sanguine mood, some un-
pleasant surprises may pop up over the
next few months. James Capel's McNei-
r's figures that capacity constraints will
limit Europe's profit growth to an
average of 10% to 12% this year. And
chief economist, Richard Freeman,
notes that high inflation and interest
rates will slow British growth by late
1989 or early 1990. In fact, some weak-
nesses already are starting to appear.
Unilever Group PLC, Britain's largest con-
sumer-electronics retailer, reported a
profit slide in the six months ended
November, and expects still worse
losses for the period ending May 30.
Even in Britain, no one is ready to
call an end to the expansion. In Brit-
ain and across Europe, corporate treas-
uries are bulging with cash. That alone
continues the investment and buyout
mania that have kept the Continent bub-
bling. Analysts have drastically under-
estimated European profit growth for
several years running. They may be
pleasantly surprised again in 1989.

*by Blanca Riemer in Paris, with Jona-
Kapstein in Brussels, John Temple-
in Bonn, Richard A. Melcher in Lon-
don and bureau reports*

Commentary/by Ted Holden

WHY TIME MAY BE RUNNING OUT FOR TAKESHITA

It was a weary Noboru Takeshita
who trudged to center stage at a
parliamentary hearing on Apr. 11
to face a tough grilling. As TV cameras
zoomed in, the Prime Minister ex-
plained his role in Japan's biggest polit-
ical scandal in years, confirming re-
ports that he had received \$1 million in
political donations from Recruit Co.,
the conglomerate at the heart of the
influence-buying affair. Takeshita even
admitted an additional \$160,000 in con-
tributions reporters had missed. But
his testimony still left people looking
for more. Are new re-
velations forthcoming?
"I am not a god," an-
swered Takeshita. "It's
very hard to say."

Takeshita's stalling—
for almost a year since
the affair first broke to
the surface—has exact-
ed a stiff toll. It has
already brought the
Diet, Japan's parlia-
ment, close to political
gridlock. Approval of
the budget has been
held up. Government
reluctance to sanction
higher interest rates
while the scandal con-
tinues may lie behind
the yen's recent 5% drop against the
dollar. And Washington frets that with
Takeshita hamstrung, Japan won't car-
ry out new initiatives to open markets.
Next month, the U.S. may formally
accuse Tokyo of unfair trade practices.

NO ESCAPE. More and more, it seems
unlikely that Takeshita can survive. An
anxious Japan is becoming tired of sor-
did carryings-on within the ruling Lib-
eral Democratic Party (LDP). One band
of renegade LDP Diet members already
is campaigning for the removal of Ta-
keshita and his Cabinet. But some ob-
servers maintain that Takeshita can't
quit because his main LDP rivals also
were besmirched by Recruit. Three
Cabinet ministers already have been
forced to quit, and newspaper reports
say three top LDP politicians and one op-
position figure may face arrest. Still, it
shouldn't be hard to replace Takeshita.
A party elder might form a caretaker
government. That's what happened
when a scandal forced Prime Minister
Kakuei Tanaka to resign in 1974.

Takeshita might try to buy time by
forcing his predecessor, Yasuhiro Na-
kasone, to go before the Diet. It was
on Nakasone's watch that Recruit's
founder, Hiromasa Ezoe, distributed
cash and stock in an unlisted subsid-
iary to politicians and corporate offi-
cials, netting them millions when it
went public in 1986. But Takeshita
risks alienating Nakasone loyalists if
he puts the former leader on the spot.
Nakasone's testimony might even
prompt more calls for Takeshita to
quit. "He can't escape," says Keio Uni-
versity professor Ya-
sunori Sone.

With the public fuming
over his recently
enacted national sales
tax and Recruit, Take-
shita's approval rating
is down to 9%. Now
some analysts believe
the ruling party's legis-
lative edge will be en-
dangered unless the
Prime Minister quits.
The LDP is already ex-
pected to take a pound-
ing in elections for the
Diet's upper house this
summer. The party
could face a bigger set-
back in the more pow-
erful lower house, where the LDP risks
losing its 40-seat majority in elections
due between now and mid-1990.

Takeshita could limit such losses by
calling for lower house elections now
and then quitting. Voters, tired of
hearing Takeshita make vague pledges
to clean up the political system, proba-
bly would view such a move as a first
step toward real reform. Takeshita's
successor then could try, for example,
to push for strict enforcement of Ja-
pan's campaign-contribution laws.

Takeshita isn't listening. He and the
LDP's other bosses would rather delay
the lower house elections until 1990,
hoping that Recruit will simply die
away. But reporters and prosecutors
show no signs of giving up the chase.
And the public is losing patience. True,
a snap election would throw the LDP
into a tizzy as it searches for a new
leader. But it faces even greater
strains if Takeshita drags his feet on
Recruit any longer. Perhaps the wisest
course would be for him to resign now.



**TAKESHITA: RECRUIT HAS COST
HIM THREE CABINET MEMBERS**

FRANCE

AVANT LE DELUGE AT MOËT HENNESSY LOUIS VUITTON

The internal battle for control may be reaching a climax

Its products are the epitome of French refinement: Dom Perignon champagne, Dior perfume, Louis Vuitton luggage. But there's nothing high-class about the bitter nine-month struggle to control LVMH-Moët Hennessy Louis Vuitton, France's largest producer of luxury goods. Now the fight is moving into a decisive phase.

Textile and real estate magnate Bernard Arnault, 39, holds financial control of the \$2.6 billion group and is trying to squeeze out his nemesis, Henri Racamier, 77, chairman of Louis Vuitton before it merged with Moët-Hennessy in 1987. Fighting back, Racamier is using the French courts and financial regulations to preserve a measure of independence for the Vuitton unit he still heads. In the background is Britain's Guinness PLC, Arnault's partner in his drive to take control of LVMH. On Apr. 6, Guinness forked over \$323 million to up its effective stake in LVMH to 24%. If the fight for LVMH worsens, the British could quietly expand their stake.

Until recently, Arnault seemed destined to rule as undisputed boss of LVMH. A former real estate developer, Arnault bought control of France's Agache-Willot textile group in 1984. In January he became chairman of LVMH after he and Guinness secured control. They now control 44% of LVMH stock and 35% of its voting shares. Arnault also has support from the Moët and Hennessy families, who hold 19%. Racamier claims to have about 30% of the votes, with institutions and the public holding the balance.

IN THE BAG? Arnault has been tripped up, at least temporarily, in his bid to oust Racamier. Arnault wanted to cut the retirement age at Louis Vuitton from 85 to 70 and restructure management, consolidating control in his hands. But an appeals court on Apr. 10 blocked Arnault, giving Racamier much-needed breathing space. A spokesman for Arnault discounts the court ruling. "It merely postpones our victory," he says.

Arnault faces another hurdle in a few weeks, however, when the French stock exchange commission is to rule on charges against him—some of which were pressed by Racamier. One question believed to be under investigation is how Arnault managed to buy up a pile of publicly traded LVMH warrants last July in a very brief period of time. The commission is investigating possible "parking" of warrants by Arnault's investment bankers. One other issue: whether



THE RICH MIX AT LVMH

Product	1988 sales	Operating profits
	Millions of dollars	
HANDBAGS, LUGGAGE	\$560	\$231
COGNAC, SPIRITS	648	214
CHAMPAGNE, WINE	774	165
PERFUME, BEAUTY	593	94
PRODUCTS, CLOTHES		
OTHER	35	-32

DATA: LVMH-MOËT HENNESSY LOUIS VUITTON

Arnault used inside information when he bought additional shares in January.

The commission's ruling on these allegations will set the stage for a showdown at a June shareholder meeting. Barring a dramatic decision against Arnault, most Paris observers still give him the edge. But Racamier will use strong performance of Louis Vuitton to woo stockholders. Racamier has made Vuitton the jewel of LVMH, accounting for 50% of profits. When he took over in 1977, the company had two stores—both in France—and sales of just \$12 million. Racamier opened 120 stores worldwide and boosted sales last year to \$841 million—32% of LVMH sales.

SCOTCH TAPE. Playing the role of patient partner is Guinness. As part of a web of Arnault investments, LVMH is the largest stockholder in the British beverage company, with a 12% stake, and Arnault sits on Guinness' board. But the interlocking companies that Arnault and Guinness have established obscure who really controls what. Guinness has actually put more money into the various corporate vehicles that Arnault uses to control LVMH than has Arnault himself. "You could say that the beneficial ownership of LVMH is now more with Guinness than with [Arnault]," says Frank Fitzpatrick, finance director at Guinness, "but control is not."

Guinness has strategic reasons for keeping \$1.7 billion committed to a 24% stake in LVMH. Guinness is the world's largest Scotch whisky maker, with sub-brands as Johnnie Walker and Dewar. Because of the slow growth in liquor, Guinness has embarked on a strategy of taking control of its distribution around the world and of seeking higher-margin brands.

Should the battle for LVMH spin out of control, however, the British giant is positioned to pick up at least a piece of the spoils. "If LVMH is threatened by a predator that looks like it's after the whisky and spirits, then Guinness would have no option but to step in," says Michael Proud, liquor analyst with Coutts & NatWest Securities in London. Guinness denies any plans to seize control of LVMH behind Arnault's back. Says Fitzpatrick: "There are no hidden agendas."

While the French government might tolerate a greater de facto role for Guinness, it would surely balk at overt British control. With Europe facing a 1992 deadline for creating one market, integrating European technology is a high priority. But such symbols of French culture as champagne and perfume are another matter.

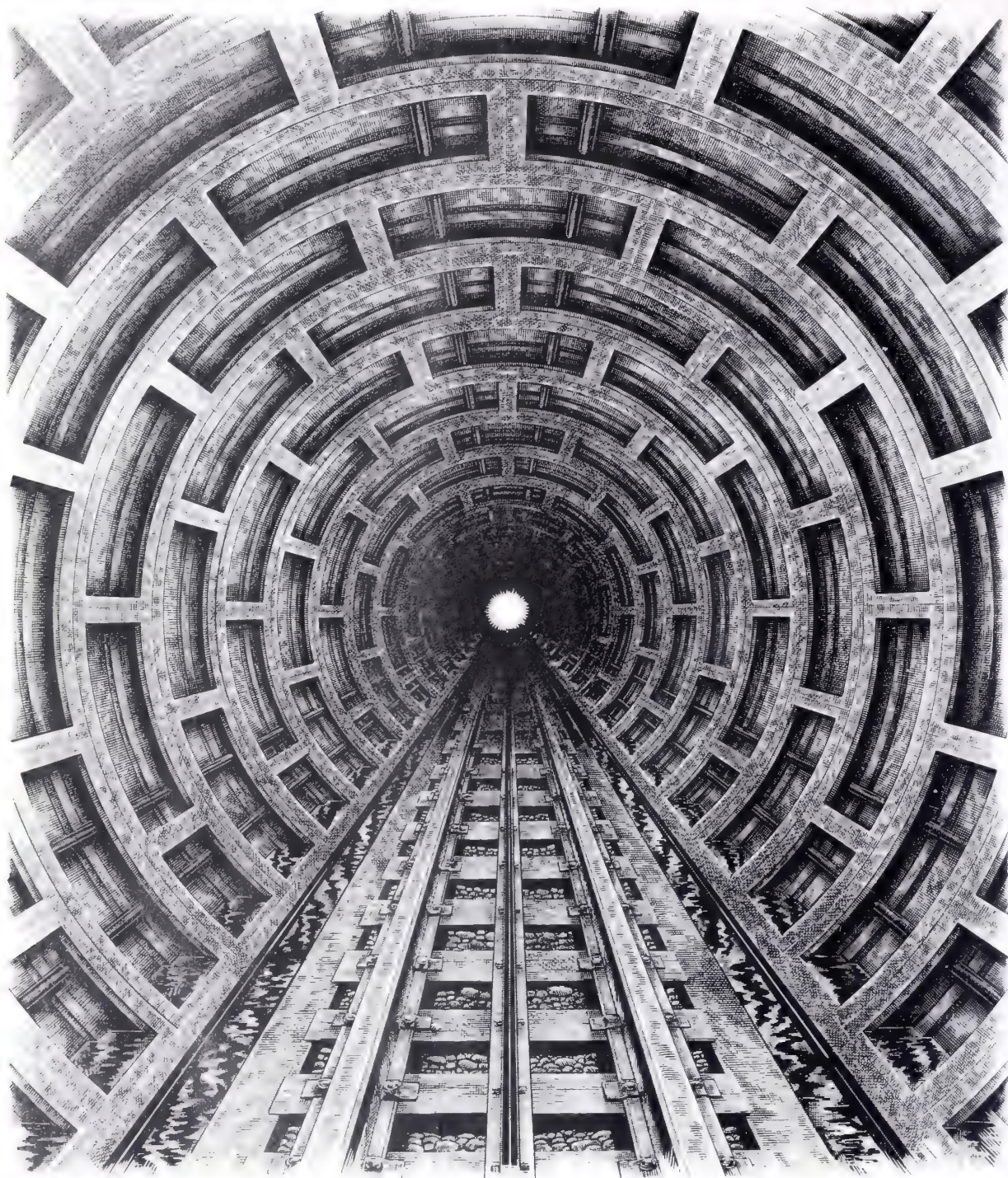
By Stewart Toy in Paris, with William Holstein in New York and Mark Maremont in London

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LIBERALIZATION IN POLAND HAS PUT BUSH IN A BIND OVER AID

To nudge Eastern European countries toward greater political and economic freedom, the U.S. for years has wielded the stick of economic sanctions and the carrot of promised rewards. Now both Poland's Marxist government and its independent union, Solidarity, are calling for aid from the U.S. and Western Europe to make a success of their Apr. 5 agreement to hold free elections and reshape the Polish economy. Solidarity members "must go to every Western capital to say that Poland is in the center of Europe and we need help," says Lech Wałęsa, the union's leader. Wałęsa will visit Rome, Bonn, and other European capitals soon, and he plans a trip to the U.S. next fall.

Such an appeal from the avuncular Wałęsa, an authentic hero of resistance to communism, puts President George Bush in a tough spot. If he stints on U.S. help, he will risk discouraging the bold and deterring reformers in other East European countries. But as a condition for any aid, the U.S. and West European governments are expected to insist that the Poles carry out painful measures to overhaul their dilapidated socialist economy. Otherwise, the reforms may fail, the attempt at liberalization in Poland may be discredited, and hopes for greater freedom in other Soviet satellites may be dashed.

ROADBLOCK TO REFORM? For cautious starters, Bush is expected to encourage U.S. business investment in Poland by authorizing the Overseas Private Investment Corp. to insure risks there. And he will agree to admit many Polish exports to the U.S. duty-free under the Generalized System of Preferences. But he is likely to take a wait-and-see attitude toward new lending to Poland by the International Monetary Fund, World Bank, and Club of Paris, the group of official credit agencies that holds two-thirds of Poland's \$39 billion debt. Poland has been hoping to get an IMF standby credit of up to \$350 million a year and about \$250 million annually from the World Bank

in order to help increase exports of hams and other products.

Poland will get little of that, however, if it fails to curb its 80% inflation and drastically restructure its decrepit, state-run industry, some of it built with money borrowed from the West more than a decade ago. The West "must make clear that we won't repeat the pattern of the 1970s and subsidize inefficiency," says Michael Mandelbaum, director of East-West studies at the Council on Foreign Relations. West Germany, the biggest lender to East Europe, is likely to take a similar approach. Axel Lebahn, Deutsche Bank's senior negotiator for East Europe, warns: "Loans have to be economically reasonable, otherwise they won't be politically reasonable."

After decades of deprivation under Communist mismanagement, however, many workers may not think a new round of austerity to win help from the IMF and Bush Administration is reasonable. A key problem, paradoxically, is that Solidarity, having been the catalyst for Poland's political opening, may now be a roadblock to economic reform. To keep the support of restless workers, Solidarity won a provision in the Apr. 5 pact for wage increases equal to 80% of the inflation rate—a mechanism that will fuel more inflation. And much of Solidarity's constituency is drawn from workers who could wreck Poland's political pact by striking to protect their jobs in obsolete industries that should be cut back or shut down. Among them is the Gdańsk shipyard where Solidarity was born.

Bush inherited from previous Administrations a U.S. policy of differentiating among East European countries by trying to reward steps toward freer markets and democracy. In Poland, his problem may be to know the difference between U.S. measures that will strengthen democracy and those that may extinguish it.

By Bill Javetski in Washington, Sylwester Kruppa in Warsaw, and John Templeman in Bonn



WORKERS ARE SAYING NO TO AUSTERITY

GLOBAL WRAPUP

HONG KONG

Confrontations between Beijing and Hong Kong's young professionals over human-rights abuses on the mainland are stirring political tensions in the once-quiet colony. The frictions reflect deepening fears that China will curb Hong Kong's freedoms after taking over the colony in 1997.

Recently a Hong Kong delegation tried to present a 24,000-name petition to the National People's Congress in Beijing that demanded the release of mainland political prisoners. Chinese officials seized the document. On Apr. 1, hundreds of protesters chanted down with one-party rule" outside the

office of Beijing's official representative in Hong Kong.

Mistrust of Britain is also growing. Political activists have asked a House of Commons committee to stop in the colony after visiting Beijing to hear their reply to China's account of its relations with Hong Kong. And colonial immigration officers provoked a local outcry by holding an expelled mainland dissident for 10 hours during his transit to the U.S. Such tensions are feeding Hong Kong's brain drain. Last year's exodus of 45,000 managers and skilled people, continuing this year at the same rate, is worsening the labor crunch and deepening foreign investors' worries.

BRITAIN

Prime Minister Margaret Thatcher is forcing a showdown with dockworkers over her plan to scrap their government-mandated lifetime job guarantees—a last bastion, she says, of restrictive labor practices. By threatening legal penalties against the 9,400 dockers, Thatcher may succeed in heading off a walkout over the issue.

The risk is that a long dock strike could trigger a recession. But Thatcher's move forces the opposition Labor Party to make a tough choice: abandoning traditional supporters or giving up its effort to show it is not dependent on hidebound unions.

THIS LAND IS WHOSE LAND?

Federal agencies are taking heat for public land mismanagement

Fly out of Las Vegas toward Arizona on a small plane, and the neon city quickly dwindles into insignificance. First there are vast sweeps of desert dotted with Joshua trees, sagebrush, and cactus. Lake Mead twinkles in the sun. Ragged mountains jut in the distance, their juniper and piñon forests sprinkled with snow.

Out here most of the land is public—administered by the federal government under a policy of “multiple use.” And signs of those uses are everywhere. Dirt roads cut through the desert. An open-pit copper mine on public land has blasted a mountain into a huge crater. A dried-out tailings pond fills a small valley with gray mud. So many white plastic pipes are driven into the desert to mark mining claims that Nevadans call them the state tree.

NO ROOM. Now, however, the management of the vast public lands in the U.S. is becoming more of a problem. Tourism, a growing population, and an increasing concern for the environment are more often at odds with ranchers and the lumber, oil, and mining companies that traditionally exploited those lands and dominated local economies. “Everyone wants to mine, log, graze, drill, fish, protect wildlife, and enjoy the wilderness on the public lands,” says Bruce E. Babbitt, former Democratic governor of Arizona and now an attorney with Steptoe & Johnson. “There just isn’t room.”

At the center of the conflict are the agencies that have stewardship over the 600 million acres of public land in the U.S., about 25% of the nation. The Agriculture Dept.’s Forest Service and the Interior Dept.’s Bureau of Land Management (BLM) and U.S. Fish & Wildlife Service are under fire from industry, Congress, and environmentalists. The General Accounting Office has churned out a series of reports faulting the agencies’ management and calling for revisions in laws that govern public lands. Members of Congress, special-interest groups—and, in some cases, the agencies’ own employees—are charging officials with suppressing data and exerting

excessive political pressure (page 52).

Ronald Reagan’s confrontational first Interior Secretary, James G. Watt, set the stage for the current uproar by advocating expanded commercial use of public land. He made available huge tracts of federal land to mining, logging, drilling, and other uses, giving environmentalists short shrift. Budgets for the agencies were squeezed, and programs for land acquisition and wildlife conservation were tabled or curtailed. Under Watt’s successors, including Donald P. Hodel, these policies persisted.

Environmentalists thought that President Bush, who declared during the campaign that he was a conservationist, might reverse some of those policies. They feel betrayed. A good many of the Bush appointees to the agencies are holdovers from the Reagan Administra-

BIG LOSSES FROM PUBLIC LANDS

► **TIMBER** The Forest Service permits loggers to cut 11.5 billion board feet of timber from national forests each year. It has lost about \$400 million annually over the last six years on the deal

► **MINING** The government sells mining claims for \$2.50 to \$5 per acre. One audit found that 12 sites being sold would net \$16,000. Their appraised value: \$14 million to \$47 million

► **GRAZING** Ranchers pay about \$2 a month for each cow they graze on public lands. Fees on private land range from \$4 up, losing the government about \$65 million a year over the past decade

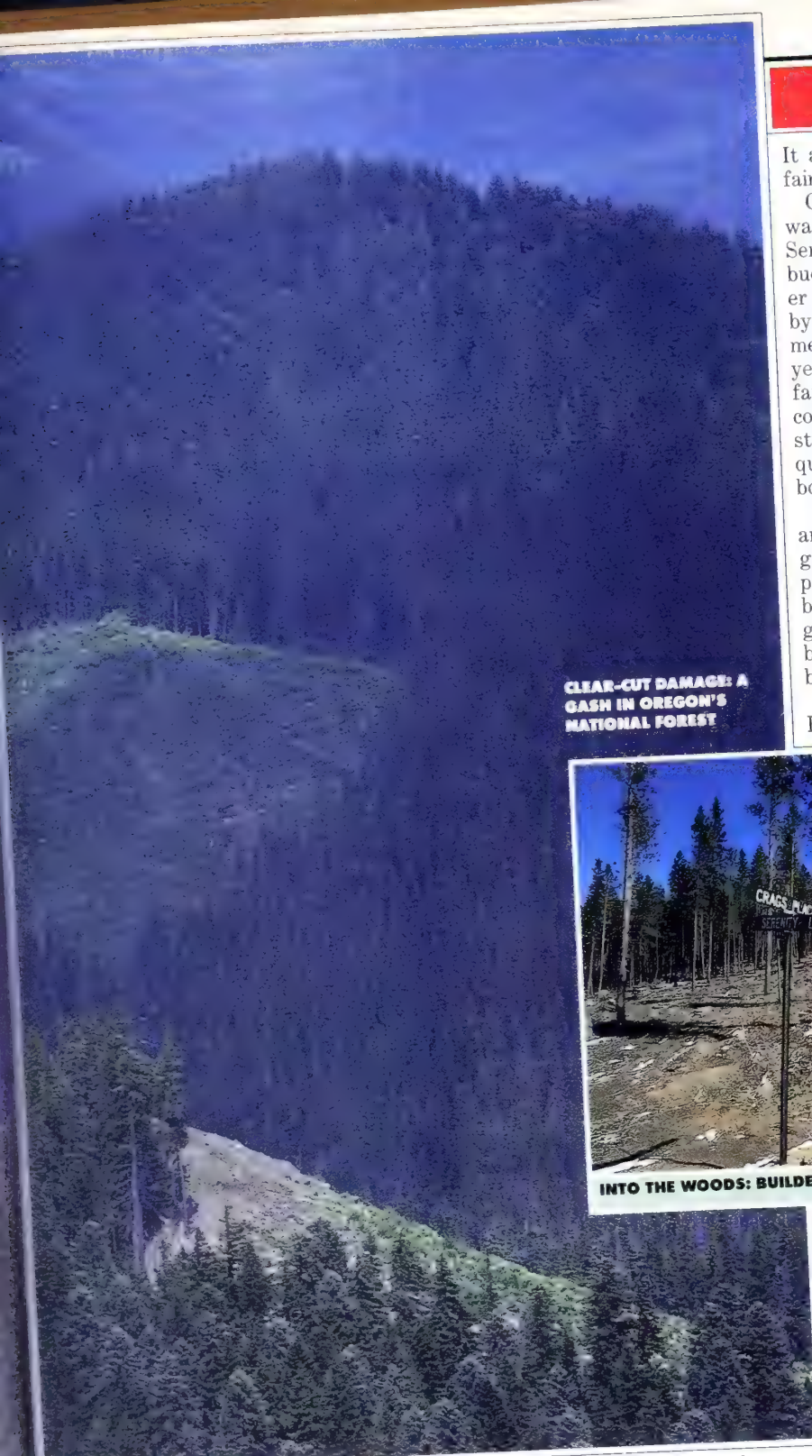
DATA: BUREAU OF LAND MANAGEMENT, U.S. FOREST SERVICE, GENERAL ACCOUNTING OFFICE, WILDERNESS SOCIETY

tion. “We prayed the era of confrontation was over. This is a nightmare completely at odds with what the public was led to expect,” says Michael J. McCloskey, chairman of the Sierra Club.

Critics are particularly riled by the appointment of Interior Dept. official James E. Cason as Assistant Agriculture Secretary, charged with overseeing the Forest Service. On Apr. 7 environmental groups said they would oppose his nomination because of his pro-development record. At Interior, Secretary Manuel Lujan Jr. has appointed some Reagan holdovers as well—and, taking his cue from Bush, supports opening the

Arctic National Wildlife Refuge to drilling.

Meanwhile, Congress is building steam for an overhaul of some land-management programs. Representative Bruce F. Vento (D-Minn.), chairman of the House Interior national parks and public lands subcommittee, has authored a bill to create an oversight commission to protect national parks from political influence. “We’ve got to get away from personalities and politics and back



CLEAR-CUT DAMAGE: A GASH IN OREGON'S NATIONAL FOREST



INTO THE WOODS: BUILDERS ARE CARVING UP THE COLORADO WILDS

professionalism in the land management agencies," he says. A House Interior & Natural Resources subcommittee is considering a bill by the committee's chairman, Morris K. Udall (D-Ariz.), that would set up a trust fund for purchasing parks, refuges, and forests. Lawmakers are eyeing revisions to mining and grazing policies.

The BLM and the Forest Service, which oversee most public lands, were not credited to preserve them. Their roots go

back to the 19th century, when the government wanted to lure settlers to the Great Plains, the Rocky Mountains, and points beyond. It wasn't until the 1970s that Congress passed laws designed to balance the needs of recreation and wildlife with development on public lands. One of them, the Federal Land Policy & Management Act of 1976, mandates that the Forest Service and the BLM manage for multiple use and consider the environmental consequences of development.

It also requires the government to get fair market value for its resources.

Critics charge that the custodians are wanting on both counts. At the Forest Service and the BLM, for instance, the budgets for wildlife, recreation, and other conservation programs are dwarfed by budgets for production and development of resources. Over the past three years, the GAO has rapped the BLM for failing to keep up-to-date records of the conditions of grazing lands, neglecting stream restoration, and failing to require many mining operations to post bonds covering reclamation costs.

Moreover, the way timber, grazing, and mineral programs are managed, the government isn't recovering the expenses it incurs from such projects as building roads into remote areas for loggers. From 1977 to 1988 the shortfall between receipts and expenses was \$31 billion, according to government figures.

Take grazing fees. The BLM and the Forest Service provide about 10% of the

nation's total rangeland. In 1987 the BLM spent \$17 million more to run the program than it made in grazing fees. This year ranchers will pay \$1.89 a month per cow to graze on BLM land, far less than the \$4 or more it costs on private lands. And trees cut from national forests supply roughly 15% of the timber cut annually. Yet the Wilderness Society estimates that the government has lost an average of \$400 million a year on timber sales since 1982.

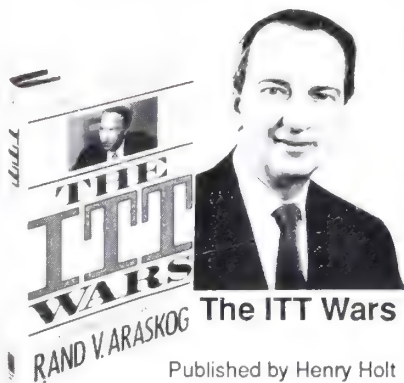
YESTERDAY'S PRICES. Under the Mining Law of 1872, which governs the mining of hard-rock minerals, anyone can stake a claim on public lands, excluding designated wilderness areas and national parks. Those who discover ore can buy the land, under the so-called patent provision, for \$2.50 or \$5 per acre—what it was worth during the 1870s.

Today, though, land values are a bit

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higher. On 12 sites studied by the GAO, the government would ring up a total of \$16,000 for land variously appraised at \$14 million and \$47 million. One 1,280-acre parcel adjacent to the Lake Mead National Recreation Area would bring the government \$3,200; a local realtor estimates its worth at \$26 million.

As Congress looks for ways to cut the budget deficit, support, at least in principle, is mounting to phase out below-cost sales of resources. "The bottom line is preventing the drain on the Treasury and ensuring the wise management of public lands," says Representative Mike Synar (D-Okla.), chairman of the House government operations subcommittee on energy, environment, and natural resources. He supports eliminating below-cost grazing, while Representative Nick J. Rahall II (D-W. Va.) is looking into revising the mining laws. Some reformers would like to see minerals under a leasing system like that used for oil and gas, where the government collects royalties on production but retains the land.

Such measures face a hard fight in Congress from Western conservatives. In the West ranchers depend on federal lands for grazing and argue that the lower fees are justified, because those lands lack fencing and other amenities. And, says Keith R. Knoblock, vice-president of the American Mining Congress, an industry group, the low cost of ore-bearing land is a necessary incentive for exploration. At the same time, some communities depend on logging in nearby national forests for their livelihoods.

But the economics of the West are shifting, and the resource industries no longer hold such enormous sway over the regional economies—or politicians. Instead, tourism and recreation, which depend on the preservation of wildlife and the scenic environment, are taking over. Arizona is still the country's copper capital, but service industries, much of them related to tourism, contribute far more to the state's coffers than mining. In Nevada tourism is the fastest-growing economic segment.

AT LOGGERHEADS. The shift is breaking down the locals' once-solid front of resistance to environmentalists. This is why Douglas Payne, who builds vacation homes, says he and his South Fork (Colo.) neighbor R. Kent Bingham, regional timber manager for Stone Forest Industries, "get along only as long as we don't talk about" logging in the nearby 1.8 million-acre Rio Grande National Forest. The logging has allowed several local mills, including Bingham's, to expand. It contributes 335 jobs and \$5.5 million a year to the local economy. But Payne insists that logging is hurting the tourist industry, which brings in \$59 mil-

lion to the six-county valley near forest. He supports Citizens for Environmental Quality, a group suing the Forest Service to roll back the cutting.

The Forest Service has made some concessions to the critics. "We need more emphasis on wildlife and recreation," admits George M. Leonard, associate director of the service. "It's a question of balance, and that balance is being addressed." He points to reduced harvests in the Bridger-Teton National Forest, near Grand Teton National Park, and the Gallatin, near Yellowstone National Park, both prime recreation areas.

But reaching a balance in the Pacific Northwest will be difficult. The coast's evergreen forests are the remnants of the virgin forests that once covered much of the country. But the federal



BISON IN UTAH: THE GOVERNMENT'S TECHNICAL PROBLEM

government is selling timber from a record 60,000 acres a year, 20% more than a decade ago. At that rate, experts predict the old-growth forests could be gone in 20 or 30 years.

Determined members of an environmental group called Earth First! are wrapping themselves around trees to stop the saws. The Ancient Forest Alliance, a coalition of environmental groups, is challenging individual timber sales under laws governing wildlife and forest management. In March environmentalists won two injunctions against new timber sales: one in Oregon against the BLM, and one in Washington against the Forest Service.

The forest industry, which employs some 150,000 people in the Northwest, is equally adamant. Any significant slowdown in logging "would throw our economy into a cocked hat," declares Dan Mumper, manager of forest resources

everhaeuser Co., who insists that such abrupt shift in raw material supply could disrupt any industry. Logging companies have vowed to sue the Forest Service if it curbs cutting; so has Washington Governor Booth Gardner.

Environmentalists charge that the Forest Service has bent to pressure from the timber industry to keep harvests high. And they claim that the inventories on which the allowable harvests are based exaggerate the amount of virgin timber still standing. During the mid-1980s, one Forest Service inventory said there were about 6 million acres of the ancient trees left on federal land. But estimates by other groups put the figure as little as 1 million acres. Last year, Wilderness Society forest ecologist Peter H. Morrison flew over some areas where trees were supposed to stand and saw only slash. The Forest Service says



LOGGING LAND ANGER ENVIRONMENTALISTS

se stands were cut after the inventory. The service is now preparing a new inventory.

In Mt. Hood National Forest near Portland, Ore., Forest Service officials did an inventory from the mid-1970s when they started to prepare cutting plans for the late 1980s and beyond. They didn't plug in data from a mid-'80s survey when it became available, because they knew it would mean a much lower harvest," says one Forest Service employee. The agency's associate director Leonard says the decision to use the old inventory was made by local managers.

COOKING DOWN. The government is also feeling heat for its management of grazelands. A GAO report last year found that the BLM and the Forest Service lacked up-to-date information on range conditions for the 268 million acres of public rangelands. Reports from the agencies, many written more than five

years ago, showed that 50% of the lands were in either poor or fair condition and therefore in danger of overgrazing, which destroys native grasses and stream habitats.

"The range is in the best condition it's been in for a hundred years," counters Billy R. Templeton, chief of the BLM's division of rangeland resources, who points out that only 7% of the rangeland is still deteriorating. Moreover, Washington officials have kicked off programs to increase monitoring of stream and range habitats and to restore damaged streams.

But even the BLM range managers doubt that directives from Washington will make a difference. While the BLM can ask ranchers to build fences, move cattle, or even cut the number of head on the range, many simply refuse. Half a dozen range managers say that, if ranchers object, BLM managers tell field personnel to back down. "Washington can issue all the paper it wants," says one. "Out here the ranchers lead the BLM around by the nose."

The land-use decisions of the government agencies also affect the comparatively small amount of land that has been set aside for preservation: the 80 million acres of the national parks. Many parks—including Glacier, Yellowstone, Great Smoky, Olympic, and Rocky Mountain—are too small to provide a self-contained habitat for many types of wildlife, which depend on the forests of adjacent federal lands.

Rapid logging of those areas—Forest Service data indicate that by 2000 trees will be felled nearly twice as fast as new ones can replace them—jeopardizes wildlife. In what's called the Yellowstone Ecosystem, a 13.5 million-acre swatch that covers three states, 60% of the grizzly bear habitat is open to cutting; more than 70% of the habitat for bald eagles is threatened by development.

Many reformers are growing impatient with the very doctrine of multiple use because it leaves too much discretion in the hands of the land management agencies. "It's synonymous with no direction administratively," says Babbitt. "It makes public lands available to everybody for everything."

Babbitt and others advocate replacing multiple use with "dominant public use," the principle of dedicating public lands to major, long-term public uses. That wouldn't put an end to logging, mining, drilling, or grazing. But with concern over the environment clearly on an upswing, there are sure to be changes in the way the government manages the land that is everyone's backyard.

By Emily T. Smith in New York, with Vicky Cahan in Washington, Randy Welch in Denver, Michael Parks in Seattle, and bureau reports

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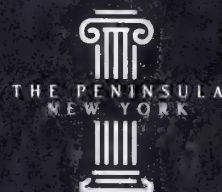
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INTERIOR IS A HOUSE DIVIDED

Bickering between branches and charges of altered reports

When it comes to his scientific opinion, Rolf L. Wallenstrom tends to be outspoken. As head of the Western Region at the U. S. Fish & Wildlife Service, the 56-year-old biologist fought to force a sister Interior Dept. agency, the Bureau of Reclamation, to replace wetlands that had been destroyed by pollution in the Kesterson National Wildlife Refuge and to increase water flowing into San Francisco Bay.

In January, Wallenstrom was fired for refusing a transfer to what he calls a "make-work position." The transfer, he says, was a reprisal for insisting on carrying out his agency's mission of protecting fish wildlife in the face of political pressure.

Wallenstrom is not the only one with that complaint. Other FWS employees charge that officials ordered reports altered, blocked comments critical of oil development, and retaliated against those who opposed the interference. Wallenstrom's two associate directors were also reassigned. "Speaking out on contested issues is very dangerous," says one FWS professional.

COVER-UP? Employee allegations, some backed by memos, correspondence, and draft versions of scientific reports, are raising concern in Washington. In March, Representative Gerry E. Studds (D-Mass.), chairman of the House subcommittee on fisheries and wildlife, launched an investigation. On Apr. 5, Representatives Barbara Boxer (D-Calif.) and Mel Levine (D-Calif.) called for a halt to oil-lease sales in California, charging Interior with a cover-up of environmental risks.

Frank H. Dunkle, who resigned as FWS director in March, denies any political reprisals and interference. "For my three years, they can't substantiate" any of the claims, he says. Under agency regulations, he points out, refusing transfers is grounds for dismissal.

But last April, Wallenstrom's office released an evaluation criticizing the en-

vironmental impact statement for oil-lease sale number 91, off Northern California, where drilling is hotly contested. The report said that the Minerals Management Service (MMS), the Interior agency that handles offshore oil development, had underestimated the risk of a major oil spill and the impact on wildlife. Dunkle signed the comments, but MMS officials challenged them, saying they could jeopardize the sale. Then Dunkle ordered Wallenstrom's office to rewrite the document. In May, a second version was substituted. The controversy over



WALLENSTROM: HOUNDED OUT OF THE FISH & WILDLIFE SERVICE?

the changes caused such a furor that the Bush Administration has appointed a task force to review lease sales.

The MMS and FWS have also disagreed over the interpretation of scientific data on the environmental impact of gravel causeways in the Arctic. Last year the FWS was set to recommend that the Army Corps of Engineers deny BP Exploration Inc. a permit to build a gravel causeway at Niakuk on the North Slope. The FWS scientists had decided that data from studies of an older causeway indicated unacceptable risks to fish. Scientists at the Environmental Protection Agency and the National Marine Fisheries Service drew similar conclusions.

After MMS officials challenged their interpretation, the recommendation to

deny BP the permit was not included in the comments that Interior sent to the Corps of Engineers. The Corps approved the causeway last October but ordered costly modifications. It also adopted a policy that could prevent building gravel causeways. Earl E. Gjeldre, Interior Under Secretary, and BP Exploration President George N. Nelson protested. The Corps agreed to reconsider.

Spokesmen for Gjeldre say he intervened because it's his role to resolve disputes at Interior. Both the MMS and BP argue that the data indicate no problems for the fish. The company also insists that alternatives to gravel causeways are so expensive that a ban could "shut down some development on the North Slope," says Roger C. Herrera, a BP special consultant. MMS plans a symposium in April to evaluate the research.

Even so, the dispute has worsened contentious relationships between Interior, the oil industry, and other regulatory agencies, including the Environmental

Protection Agency and the Army Corps. One Army official says that the "conflict has been rolled" by political pressure.

'GOOD SCIENCE.' In March, Gjeldre named a science adviser to speak for Interior on fish and wildlife concerns relating to causeways. Says an FWS official: "We're viewed as a threat—it's only a matter of time before we're removed entirely from assessing impacts on fish and offshore oil development." Interior officials say their actions are consistent with procedures. But in the past the FWS was Interior's voice on fish and wildlife matters. "We've always been able to state our view clearly without a problem," Felix E. Smith, an environmental assessment expert at FWS. The goal, he says, should be "to look at good science and get it in policy, not change science because somebody doesn't like the answer."

It will be up to Interior Secretary Manuel Lujan Jr. to resolve the complex of agency professionals. He can be expected to pay "more attention," say a chief aide, to their concerns. But Lujan is also a consensus manager who views his role as blending the disparate views of the agencies under him. And that still means balancing the protection of fish and wildlife against the need for development.

By Emily T. Smith in New York, with Vicky Cahan in Washington



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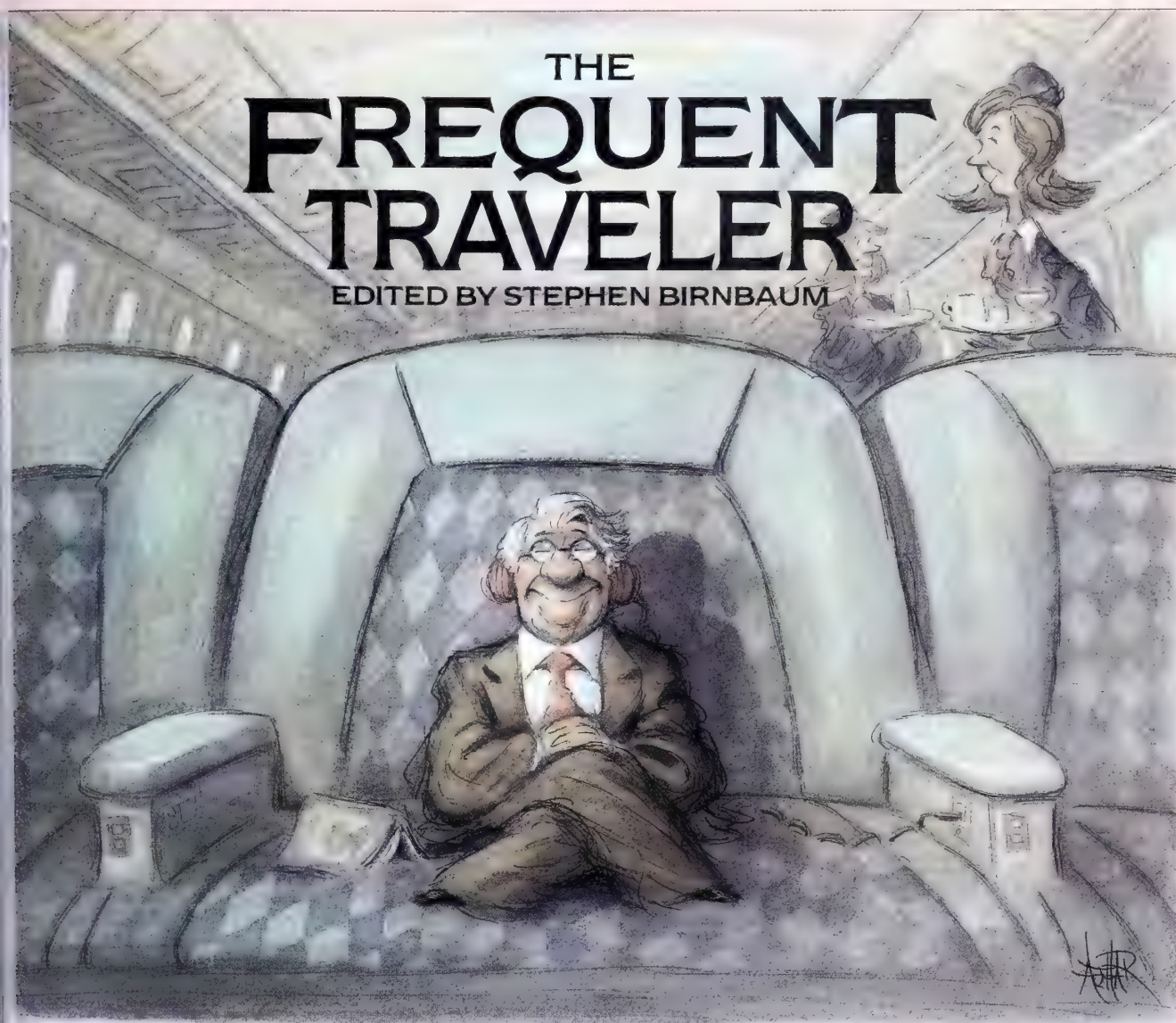
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II	Sports Season Start-Up
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IV	The Traveling Photographer
V	The Airlines of Asia
VI	Purchase Protection: Should You Leave Home Without It?
VII	Brunching It
VIII	Top of the Rental Line

I BIG BIRDS

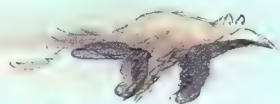
HIGH-CAPACITY, LONG-RANGE JUMBO JETS
ARE THE WAVE OF THE FUTURE IN THE SKIES

People who fly—both business and pleasure travelers—usually opt for a non-stop flight when one is available, and attitude studies suggest that most airline passengers feel safer and more comfortable on wide-body aircraft. In the years ahead air travelers will increasingly find themselves boarding bigger planes that fly farther with fewer stops en route. But it would be disingenuous to

assume that consumer preference alone is the driving force behind airlines' fleet-expansion plans or aircraft manufacturers' designs.

The considerable size and range of Boeing's new 747-400 (which went into service early this year), McDonnell Douglas's MD-11 (which will debut in 1990), and Airbus Industrie's A340 (due for delivery in 1992)

FREQUENT TRAVELER



were dictated chiefly by other market forces: economies of scale (it's less expensive to fly one big plane than two or three smaller ones), growing airport and airways congestion (a wide body consumes a single takeoff and altitude slot—the same as a small plane), and perhaps most important, the emergence of the Pacific region as an economic titan, with its long air routes to North America and Europe.

Still, consumer satisfaction is more than a nifty by-product of the new aircraft being rolled out in Seattle, Long Beach, and Toulouse. Competition for the business traveler's patronage has reached levels unknown in the history of commercial aviation. Airlines feel the pressure not only to fly the passenger safely and economically along the world's longest air routes but to get him to his destination feeling fit, well-fed, and relaxed.

ENTERTAINMENT TONIGHT

Designs for the new generation of long-range wide bodies include some exotic ideas intended to make air travel a less stressful endeavor. Multichannel, flat-screen entertainment systems installed on seat backs or armrests will allow passengers to tune in to movies, television programs, documentaries, or language lessons. British Airways has already inaugurated such a system in a quartet of its planes that fly the Atlantic, and

several other airlines have tested systems (Japan Air Lines is now installing flat screens in the first and business class sections of all its 747-400s). Initially, BA will offer passengers a choice of 50 videocassettes, and IAL will offer four channels of programming, which can be expanded to six.

Further along, the private companies that produce these systems envisage seat-back business-and-entertainment setups that allow passengers to run computer programs, reserve and cancel airline, hotel, and car-rental reservations, send and receive fax messages, or make international phone calls. Passengers will also be able to review in-flight menu selections on their screens, ordering food and drinks with the push of a button.

Competition for business travelers' favor also means that most of the mammoth new aircraft will not be outfitted with the high number of seats they're capable of holding. The 747-400, for example, can carry as many as 600 passengers in an all-economy class configuration. But most airlines will fly the new jumbo with only 375 to 450 seats throughout first, business, and economy classes.

Larger overhead storage bins, streamlined interiors, and better ventilation and cabin lighting are also among the passenger-friendly details found in the new generation

of long-range wide bodies. Travelers may not be invited to stretch out in new crew "dormitories," but at least the rest quarters should make for more relaxed, attentive pilots and flight attendants on nonstop flights that will last up to 16 hours.

These are heady times for aircraft builders and expensive times indeed for the airlines. So in demand is the newest edition of Boeing's venerable 747 that even if an airline wanted to spend the \$110 million to \$129 million sticker price, it would have to wait one to two years for the jumbo to be delivered. Despite the astronomical costs and long waits, the major international carriers continue to deluge Boeing with orders for the biggest plane of them all. JAL and Singapore Airlines each have orders and options for 20 of the new jets. Australia's Qantas is taking 20 of the planes, Air France 28. And British Airways will pay a record \$4.1 billion for 31 of the 747-400s. In all, 22 airlines and leasing companies, half of them based in the Pacific region, have placed orders or options for some 240 of the jumbos.

Not surprisingly, Boeing just had its best year ever. The company will be increasing production of the "400" (actually it's the fifth version of the jet, which was introduced in 1969) from four to five planes per month. The backlog of orders continues to mount this year—as many think it will—the company may have to build a new plant just to keep up with demand. Without a competing jumbo on the horizon, however, Boeing hopes to avoid such an investment and the risk that a new facility could go idle early next century. For now, the company is betting the airlines will wait years for a 747-400 rather than settle for a lesser wide body.

RIVALS IN THE SKY

But Boeing may be feeling some heat from old rival McDonnell Douglas. The MD-11, a derivative of the three-engine DC-10, will be available beginning next year. Although not as large as a 747 (the MD-11 will carry 323 passengers in a three-class configuration—4 more than a DC-10), it can fly the long international routes that airlines also have in mind for the new Boeing plane. These include Los Angeles-Hong Kong, New York-Tokyo, and London-Sydney. For added capacity, McDonnell Douglas has stretched the DC-10 fuselage by more than 18 feet. If the airlines show an interest, the firm says, it could build (by the mid-1990s) a super-stretched, long-range MD-11 that would carry about as many passengers as Boeing's latest jumbo.

Not to be entirely outshone by the new 747-400's imposing upper deck (which most major carriers will outfit with about 60 business-class seats), McDonnell Douglas is offering an optional Panorama Deck below the first-class cabin, in space that would otherwise be used for cargo or baggage. The new low-

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deck takes its name from the slight downward tilt of the passenger windows, which will afford ground views never before available to commercial air travelers. There's little to see from 40,000 feet above the Pacific, but take-offs and landings should be an eyeful.

So far, airlines have placed orders and options for more than 250 MD-11s. American alone says it may take as many as 50 of the planes, and Delta 40, with Swissair, Finnair, and Thai International among the other customers.

Meanwhile, Airbus Industrie is breathing down the Californians' necks with a 1992 delivery date for its A340, a four-engine, long-range (a full 9,000 miles) wide body with three class seating for 290 passengers (and all-economy seating for up to 440).

With the A340, the European consortium actually gets two new planes to sell. A two-engine version of essentially the same plane—dubbed the A330 and due for delivery a year later—will vie in the medium-range market. Northwest, the first airline to fly the Boeing 747-400 earlier this year, will also be the first U.S. carrier to fly the A340. Other

orders have come in from Air France, Lufthansa, Iberia, Royal Jordanian, TAP Air Portugal, and UTA. All told, Airbus has 71 firm orders for the A340, with options on another 39, and the A330 version has chalked up about half as many orders and options.

Industry experts estimate that airlines need as many as 5,700 new jets over the next decade—half of them wide bodies. So great is the demand for new aircraft—to replace aging, inefficient planes and to serve new markets—that all of the new long-range wide-body models could turn out to be profitable for their builders.

SKY TECH

What comes next? The airlines' foremost concern is to acquire planes of all sizes that burn less fuel and require fewer pit stops for maintenance. New aircraft designs will increasingly rely upon lightweight non-metallic composite materials, on-board computers, and new engine technology to accomplish these goals. The consumer has a stake in this endeavor. When planes are less expensive to operate, high purchase costs

are offset, which eases the upward pressure on airfares. But fuel-burn ratios aren't very sexy stuff. Business travelers are more inclined to wonder whether airplanes will get bigger and faster.

Bigger, certainly. Until recently, industry experts spoke of a double-deck, 1,000-passenger 747 as a theoretical possibility. Now they're beginning to sound as if such a *jumbo jumbo* is almost inevitable; that one could traverse the Atlantic and Pacific regions well before the end of the 1990s. So massive a commercial jetliner augurs intriguing new approaches to long-haul flights. In particular, the three standard classes of service could expand to four, five, or even more. There's room for growth at both ends of the fare spectrum: High-density cabins could be installed for passengers paying the lowest discount fares, while ultrapremium, first-class cabins (including sleeping quarters and private compartments) might lure high-paying executive travelers. In-flight business centers, cabins for travelers with children, and even buffets or snack bars are also among the possibilities.

A few tentative moves have already been made in this direction. From 1983 to 1987, on some of its 747s, Korean Air in effect had four classes: a cabin for discount passengers at the back of the plane, a business class cabin for full-fare economy passengers, a souped-up business class at the front of the plane for those paying a premium fare, and first class on the upstairs deck. Several years ago Philippine Airlines installed sleeping berths in its 747 "bubbles" (the upstairs decks), and McDonnell Douglas will offer a Pullman-type sleeper cabin as one version of its downstairs Panorama Deck on the MD-11.

Will the new aircraft fly faster? Maybe. Current-generation jets already fly just a fraction below the speed of sound, so there's nowhere to go but supersonic. As the Concorde has proven, breaking that barrier with commercial transports is possible but risky and outlandishly expensive.

Certainly, former President Ronald Reagan's dream of a commercial "space plane" dubbed Orient-Express—a suborbital craft that would carry business travelers from New York to Tokyo in less than two hours—will not be built until well into the next century, if ever. But all of the world's major aircraft manufacturers are working on more modest plans for a new generation of supersonic jet transports.

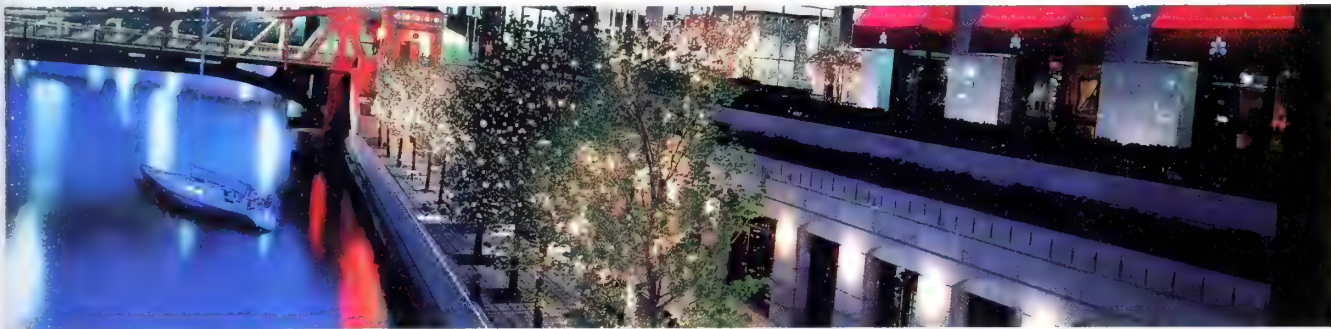
SON OF CONCORDE

Aerospatiale, a French firm that joined with the British Aircraft Corporation to design and build the Concorde during the 1960s, wants to move quickly on a 200-passenger AST (advanced supersonic transport) that could fly at speeds slightly greater





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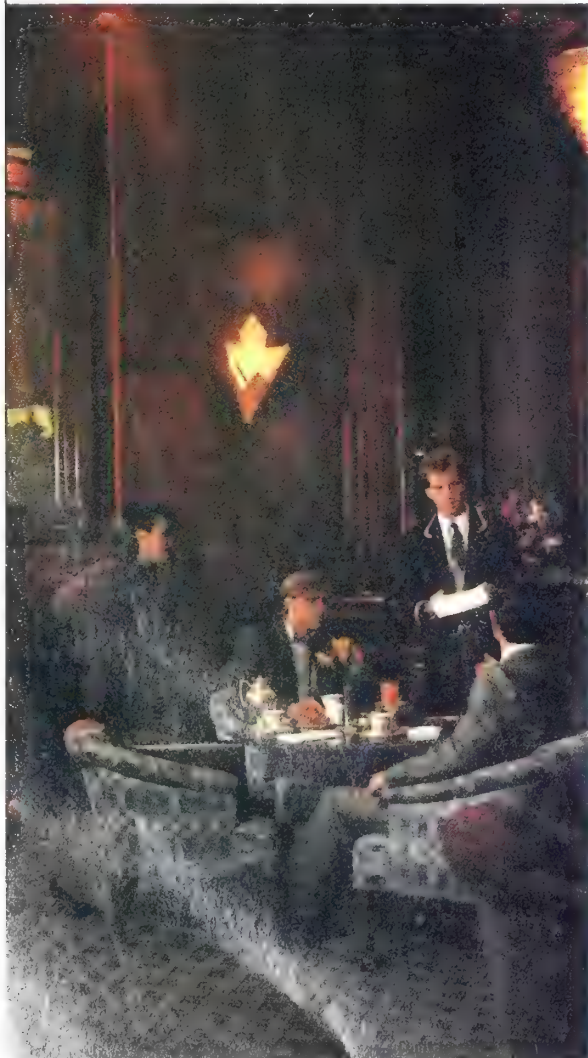
than Mach 2, or twice the speed of sound. Such a plane would be as fast as the Concorde and carry twice as many passengers, but a lot of American, British, and Japanese experts think it's still too small and too slow.

Boeing and McDonnell Douglas engineers are beginning to look at planes that could carry wide-body loads (as many as 300 passengers on transatlantic and transpacific flights) at speeds in excess of Mach 3. Even more ambitiously, Japan is working on designs for a Mach 5 engine that would burn

liquid methane rather than traditional jet fuel. Such a radically new engine, the Japanese say, could be tested as early as 1995.

Any Son of Concorde will be a massive undertaking. Not only will the plane have to be big and fast with an exceedingly long range, it will probably have to fly over continents at supersonic speeds without shattering windows and nerves below—and without damaging the ozone layer of the upper atmosphere. Some industry insiders believe all of this can be accomplished before

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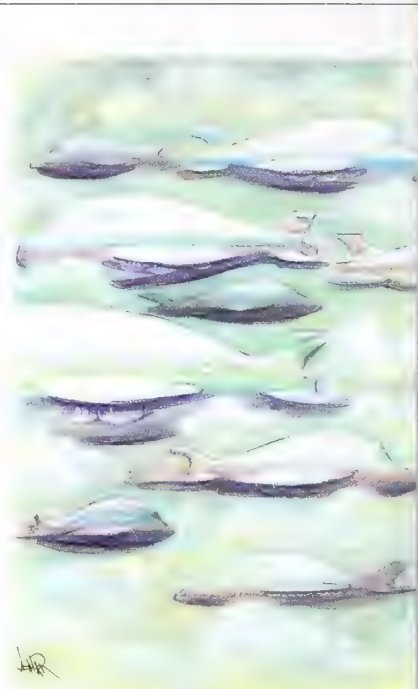
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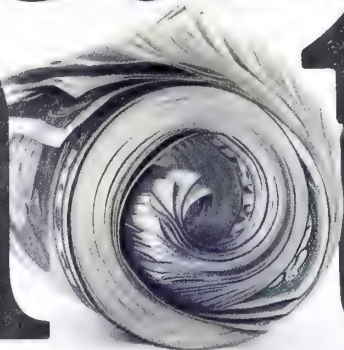


the year 2000. And by 2015, one Boeing study suggests, a third of all intercontinental passengers could fly to their destinations at supersonic speeds. Others, however, see both projections as overly optimistic. Whenever it's built—if it's built—the next supersonic will almost certainly be a multinational project, combining the ideas and financial resources of Europe, Japan, and the United States.

It may also be the first of the big high-capacity planes to be widely flown in a genuine high-capacity configuration. As the Concorde has proven, business travelers will forfeit the usual roominess of a first-class cabin and pay higher than first-class fares to race to their destinations faster than a rifle bullet. Since it's doubtful that an airline would see a future SST (supersonic transport) as anything but a single-cabin, premium-class plane, don't expect lounges, business centers, sleeping berths, or for that matter, commodious legroom. (It's ironic that travelers will accept close quarters only at the lowest and highest ends of the fare spectrum.)

The 747-400, MD-11, and A340 may be promoted by their builders as high-capacity planes, but few business travelers will ever experience all the cramped possibilities. Only IAL—which for 15 years has shuttled 500-plus passengers between Tokyo and Osaka in all-economy class 747s—and a few charter carriers have shown much interest in outfitting subsonic wide bodies with all the seats that design specifications and engine thrust permit. While some market forces push subsonic aircraft ever larger, other demand added comfort, less confinement, and increased seating options. Competition for the frequent traveler's business has airlines shopping not only for bigger planes but for better planes.

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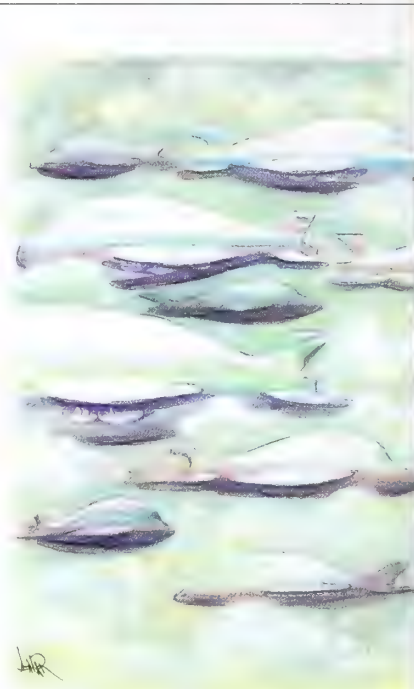
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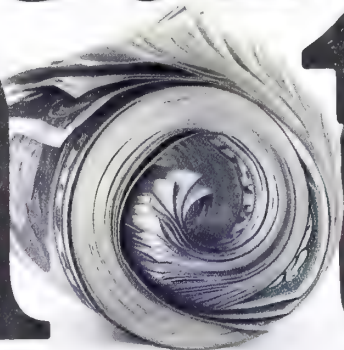


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Marriott's Castle Harbour Resort
(Tulsa, Okla.)

Originally built in 1931 as a stopover for cruise passengers traveling between the United States and Britain, this elegant 250-acre resort recently underwent a \$60 million renovation and expansion. Dramatically perched on a cliff 100 feet above an Atlantic Ocean inlet, the original, traditional-looking structure now includes a terraced addition

worthy of the Jetsons, the two contain a total of more than 400 rooms. Tennis takes a back-seat to golf at Castle Harbour, with only six courts, but those six are great. The resort's 18-hole golf course has a spectacular setting, overlooking the ocean from many vantage points. Its 6,400-yard, par 71 layout was designed by Robert Trent Jones, Jr. In addition, there are two beaches and a private dock. (Call 800-228-9290 for more information.)

Pinehurst Hotel and Country Club
(Pinehurst, North Carolina)

"It's a beautiful day at Pinehurst. How may I help you?" asks a soothing voice at the other end of the phone line. The greeting alone is enough to encourage would-be travelers to make haste to the nearest airport. Indeed, the hospitality at Pinehurst, in North Carolina's Sandhills region, is constant. While the prevailing attitude there is one of relaxed and gracious living, Pinehurst also serves as one of the most highly regarded sports destinations in the country.

Back in the early 1900s, lawn bowling and croquet were favored here (they're still avail-

able), and Buffalo Bill's Wild West Show. Annie Oakley was an instructor at the famous Gun Club. Today golf and tennis reign. Of Pinehurst's seven championship courses (comprising 126 holes—more than any other single resort in the world), the favorite hangout is Course 2, built by the legendary course architect, Scotsman Donald Ross. With greens that recently have been converted to the finest turf grass (Penncrest Creeping Bentgrass), Course 2 is once again in rare form. Course 7, the newest layout adjacent to the PGA Hall of Fame, is a Ross Jones-designed course beloved (and cursed) for its array of water hazards. Weekend- and week-long golf instruction programs focus on honing skills through videotape evaluation.

Tennis mavens have their choice of 10 HarTru and 10 hard courts at Pinehurst, which was awarded *World Tennis Magazine's* five-star designation for excellence. A weekend- and week-long Tennis Advantage School guarantees unlimited court time and culminates in a tournament and awards ceremony. Instructors concentrate on footwork and stroke techniques, and also make use of video playback. The tennis director is former touring professional Jim Ward. (For information on the schools call 800-634-9297; in North Carolina, 800-458-4711. For reservations call 800-334-9560; in North Carolina, 800-672-4644.)

The Cloister
(Sea Island, Georgia)

This place is aptly named—composed of two islands that contain five miles of private beach, it may be the ultimate retreat. A collection of low, sun-baked, vanilla-colored buildings with red-tile roofs sets the tone. On Sea Island. Adjacent St. Simon's Island is the site of the former Retreat Plantation. Retreat was the center of a lucrative cotton business prior to the Civil War, and a few remaining ruins serve as reminders of that era: an old slave hospital and a burial yard. But rather than focus on the past, the Cloister does a sensational job of entertaining its visitors here and now. Tennis and golf are among the prime activities at this resort, which earned the Mobil Five-Star and AAA Five Diamond awards both this year and last.

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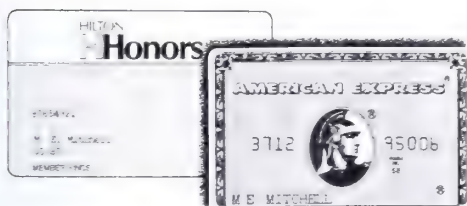
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An avenue of stately oaks announces the entrance to the Sea Island Golf Club, a 36-hole spread of four tremendous nines. Guests have access to an 18-hole layout on St. Simon's Island, too. Also on the ball are the Cloister's tennis options: 18 clay courts, primed twice daily, plus a singles practice court that automatically returns balls to players in a variety of ways. Visitors who opt for the tennis package are guaranteed at least two hours of court time daily—even in spring and summer, the busiest seasons. (Call 800-SEA-ISLA for more information.)

Amelia Island Plantation (Amelia Island, Florida)

When I came to visit Long Point's proposed site, I was impressed with its vegetation and natural elevation, but I was also concerned that the course not be overly severe or difficult," says Tom Fazio, architect of Amelia Island's newest and perhaps most highly respected 18-hole layout, which opened just over a year ago. Fazio saw immediately that the area's rugged landscape—which determined the scope of the challenging course—was its prime appeal.

Guests at the 1,250-acre Amelia Island Plantation (which has 1,300 rooms and

condos of diverse sorts) are similarly impressed by the natural beauty of this northernmost barrier island off Florida's east coast. Teeing off on the 45 holes—which border the Atlantic, are buried deep among oaks and maples, or are obscured in marshland—and hitting forehands under moss-draped magnolias are two of this Mobil Four-Star resort's main attractions.

World Tennis Magazine awarded Amelia's 25-court complex five stars in 1988, and *Golf Magazine* called it one of the top 12 golf resorts in the United States. The other blockbuster layout here is Pete Dye's Amelia Links, a collection of 3 nines appropriately named Oakmarsh, Oysterbay, and Oceanside.

If a golf club or tennis racket is not yet a natural appendage, there's also a four-mile stretch of white sand beach perfect for crabbing, horseback riding, bicycling, or just plain loafing. (For information call 800-874-6878.)

The Marriott at Sawgrass/ Marriott's Bay Point Resort (Ponte Vedra Beach, Florida)

Sawgrass has been an exclusive residential community for 12 years, but now guests at these two Marriott properties can also reap the benefits of its spectacular location and

golf and tennis facilities. Sandwiched between the Atlantic Ocean and the Intracoastal Waterway, and equidistant from Jacksonville and St. Augustine, Sawgrass is home base for both the PGA Tour and the Association of Tennis Professionals—not exactly Little League stuff. In fact, Sawgrass boasts that it's America's second largest golf resort, with 99 holes, five championship courses, four driving ranges, and eight putting greens. Pete Dye's Stadium Course is the standout there—*Golf Digest* magazine rated the 6,857-yard, par 72 monster one of the top 25 resort courses. Its well-known island hole (#17) requires golfers either to sink or swim—the must clear a lagoon with a brisk breeze often blowing in their faces. Bay Point offers two more fine courses.

The tennis center at Sawgrass features ten HarTru courts, four of which are lit for evening play. ATP's separate training facility (noted for its exercise and sports medicine clinics) is building 14 grass, red clay, and hard courts. On the grounds of Bay Point are an additional 12 Rubicon HarTru courts. And on a more relaxing note, Sawgrass sports the only official croquet court between Palm Beach and Savannah, along with two whirlpools situated atop waterfalls and lagoons. (For more information call Marriott at Sawgrass.)

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at 800-872-7248. Contact Marriott's Bay Point Resort at 800-874-7106, in Florida, 904-234-3307.)

The Lodge of Four Seasons

(Lake Char, Missouri)

In central Missouri, about halfway between St. Louis and Kansas City and overlooking Lake of the Ozarks, is this 7,200-acre golf-and-tennis playground, which deserves special kudos for its instructional programs. Duffers and greens' connoisseurs alike will appreciate every one of the 18 holes at the Robert Trent Jones, Sr.-designed course, which *USA Today* named as one of the top ten resort courses in the country. There's also a nine-hole layout and an indoor driving range. The Golf University, opening next month, was conceived in part by Ken Blanchard, coauthor of *The One Minute Manager*, a best-selling self-help manual for aspiring business tycoons. The school's player-to-pro ratio will never exceed six-to-one.

The tennis scene at the Four Seasons is equally impressive. The 23-court complex is the site of Dennis Van der Meer's highly acclaimed Tennis University (Billie Jean King once called him "the world's greatest tennis coach.") Its popular three-day, ten-hour clinic is held a few times each month. In addition,

the health and fitness center offers innumerable state-of-the-art machines and conveniences, and the glorious Lake of the Ozarks is the site of a plethora of water activities. (Call 800-THE-LAKE for more information.)

Lakeway Resort and Conference Center

(Austin, Texas)

Nestled in the Texas Hill Country amid white limestone cliffs and spring-fed valleys, this hideaway has white-tail deer and wildflowers on its grounds. Lake Travis, its 65-mile-long namesake, accommodates everything from waterskiing to reclining on a pontoon, and anything in between. And Lakeway does just as well by tennis and golf fans.

The Jack Nicklaus-designed Academy of Golf and the World of Tennis, both top-notch educational facilities, are two of the resort's finest assets. Fifty-four holes of golf and 32 tennis courts—including the stadium court, which boasts a 1,200-seat arena—round out the picture. As a final fillip, a racket-shaped swimming pool is one of three that welcome guests after a hot day on the courts or the courses. (Call 800-LAKeway for information.)

Pebble Beach Resorts

(Pebble Beach, California)

California's legendary 17-Mile Drive winds

through a forest and then skirts the dramatic Monterey coastline, where surf crashes ceaselessly against the rocky shore. While the short, breathtaking journey could be reason enough to visit, for most travelers it's only the approach to what may rank as the nation's foremost golf site, Pebble Beach. The complex consists of two luxurious hotels—the Inn at Spanish Bay and the Lodge at Pebble Beach—and four superb golf venues: Pebble Beach Golf Links, Spyglass Hill, Del Monte, and, the newest, the Links at Spanish Bay, a Scottish-style course with sand dunes reaching 24 feet. Television viewers will no doubt recognize the scenic Pebble Beach course, designed by Jack Neville, on which many national tournaments are held annually. (The U.S. Open Championship will be played there again in 1992.) It extends along Carmel Bay right to the edge of the studded town that once elected Clint Eastwood its mayor.

Both hotels tip their hats to the tennis crowd, too. The Inn's tennis pavilion has eight plexi-pave courts in a garden setting on the Spanish Bay coastline; and at the Lodge, the Tennis Club features 14 plexi-pave courts (including a stadium court). Clinics and lessons are available at both locations. (For more information call 800-654-9300.)





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THE ARRIVAL OF THE AIRPORT HOTEL

BUSINESS IS BOOMING RIGHT OFF THE RUNWAY



Anchorage's Clarion Hotel is situated on the shore of Lake Spenard, the world's premier floatplane base.

The term "airport hotel" used to be a slur. It described those perfunctory motor-inns-with-coffee-shops that catered primarily to a captive audience of stranded travelers too tired to care—or even notice—where they slept. In recent years, however, business-travel patterns have altered drastically. Meetings have moved away from downtown areas, industrial centers have migrated outward, and airport hotels—now uttered proudly—have risen to the occasion.

These hotels—both those located within airports and those only a short shuttle ride away—have become magnets for all sorts of business functions, and they are also the fastest-growing segment of the U.S. lodging industry. Executives and meeting planners choose them because they're convenient for fly-in attendees and far removed from urban distractions. Accordingly, many airport establishments now specialize in meetings, usually brief ones ranging from daylong conferences with overnight stays to three-day seminars. Newer properties boast an extensive selection of facilities—from such meet-

ing spaces as grandiose ballrooms or intimate boardrooms to an array of first class audiovisual equipment and a staff of specialists adept at pulling it all together.

Industrial drift away from inner cities toward airport areas and even more remote hinterlands has also spurred the development of airport hotels. The world's busiest airport, O'Hare International, is surrounded by Chicago's northwest suburbs, a booming commercial center. Newark International serves the numerous industrial enterprises of northern New Jersey and the high-tech plants around Princeton; and the San Francisco airport is an hour closer than the city itself to Silicon Valley.

EXECUTIVE RESORTS

In addition to all of the business-related amenities they offer, airport hotels accommodate the demanding corporate trade with opulent decor, a multitude of services and recreational options, and deluxe concierge levels. In terms of design, the new breed of airport habitats are just like luxury down-

town properties, with one striking addition. Exterior walls are specially soundproofed and windows are triple-glazed to keep out the noise of air traffic above and highway traffic below. First class establishments invariably provide complimentary 24-hour airport shuttles and, for those travelers with inconvenient schedules and jet-lagged digestive systems, 24-hour room service. These hotels also regularly telecast flight information, guestrooms and public areas, and some have airline check-in counters right in the lobbies.

By striving to fulfill all of a businessperson's diverse needs, the best airport properties have become self-contained executive resorts. Most have at least three restaurants, a selection of watering holes, and nightclubs presenting ambitious and imaginative forms of live entertainment. Indoor pools and fully equipped health clubs are de rigueur; outdoor pools, racquetball and tennis courts, and golf privileges at nearby courses are frequently on hand. And the most efficient hotels operate business centers that provide

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secretarial, postal, and courier services, along with typewriters, computers, photocopiers, fax machines, VCRs, and pretty much all the other comforts of the home.

Let's not overlook the bottom line: it's worth noting that rooms at airport hotels cost considerably less than those at comparable downtown properties—a discount of roughly \$18 a night nationwide. And that doesn't include the fortunes in taxi fares and the precious time lost in just getting downtown. Airport hostilities become even better deals on weekends, when business travelers go home and bargain packages abound.

All the major hotel chains are making their presence felt in and around the airport. From east to west, here are some of the top spots that are turning the airport into the place to do business.

AMELIA, WHERE ARE YOU?

New York City's airport hotels are relatively unimpressive; the standout, however, can be found across the Hudson River in New Jersey. The anchor of the \$150 million Airport City redevelopment project, the **Vista International Hotel—Newark Airport** (1170 Airport Blvd., Elizabeth, NJ 07201-2114, 800-445-8667

in New Jersey, 201-351-3900) is perfectly situated for guests with business in Manhattan (only 16 miles away) or in booming northern and central New Jersey. Open since September, the hotel is strategically positioned so that all 376 rooms have views of either Manhattan's incomparable skyline or Staten Island. An Executive Business Center has fax machines, photocopiers, VCRs, a travel agency, packaging and courier services, postal facilities, and even portable cellular phones. The lounge is called *Amelia's* after the long-lost Ms. Earhart, and its staff dresses appropriately in aviator-style uniforms. The *Newark* restaurant highlights wine and food from New Jersey (the Garden State), and for those executives rushing for a plane or conference, it serves a special three-course "55-minute luncheon."

Close to Dulles Airport and less than 20 minutes from the Pentagon and downtown Washington, DC, the **Sheraton Premiere at Tysons Corner** (18661 Leesburg Pike, Tysons Corner, VA 22180, 800-325-3535, in Virginia, 703-448-1234) caters principally to people doing business with the Feds and associations that convene near the nation's capital. It's an impressive structure; the public spaces feature polished marble floors and

crystal chandeliers, while the 445 guest accommodations are divided between high-rise glass tower and terrace rooms surrounding a large courtyard. Corporate groups can choose from among 25 meeting rooms, including 3 plush boardrooms with marble—once again—conference tables. The state-of-the-art health club boasts whirlpool, sauna, and three racquetball courts.

Situated barely a mile from Atlanta Hartsfield International Airport, the new, remodeled 496-unit **Ramada Renaissance** (14736 Best Rd., College Park, GA 30333, 800-228-9898, in Georgia, 404-762-7676) is a paradigm of the contemporary American airport hotel. The lobby is the ground floor of a spectacular seven-story atrium complex with bubble-shaped glass elevators. The premises encompass an indoor/outdoor pool, a fully equipped health club, and the luxurious Renaissance Club concierge level. To keep guests from wandering too far off the reservation, evening activities at the *R & Nite Club* consist of such antics as big-screen trivia contests, real-life versions of TV's "The Dating Game," and even executive Olympic

The **Viscount Hotel—Miami** (15301 North 36th St., Miami, FL 33166, 800-255-305



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in Florida, 305-871-6000) puts its 23-acre airport setting to especially good use with landscaped gardens, a tranquil private lake and an Olympic-size pool. The grounds also have facilities for tennis, basketball and handball, and the 18-hole Miami Springs championship golf course is right next door. The 307 guestrooms of the Trusthouse Forte property all overlook either the golf course or the airport. There are nonsmoking floors and private Executive Floors where hospitality lounges serve complimentary continental breakfast in the mornings and wine and cheese in the evenings.

The brand-new (it opened last month) **Radisson Hotel—Detroit Metro Airport** (8000 Merriman Rd., Romulus, MI 48174, 800-333-3333, in Michigan, 313-729-2600) was built mainly for groups of any size and travelers with business in nearby Dearborn—world headquarters of Ford—Ann Arbor and downtown Detroit, just 30 minutes away. The striking facade of the 11-story, 365-room property features steeply pitched glass walls that slant down over the lobby atrium and an inviting indoor pool. Some rooms have balconies overlooking the atrium; all offer the blessing of remote-control cable TV sets.

CHICAGO CHECK-IN

We'll aware of the business travelers

intense dislike of waiting in line, the **O'Hare Marriott** (8535 West Higgins Rd., Chicago, IL 60631, 800-228-9290, in Illinois, 312-693-4444) checks in its guests on the airport shuttle van. En route to the hotel, a clerk equipped with a printout of arriving guests takes a charge-card imprint, checks the information via mobile phone with the hotel and directs guests to a special counter in the lobby, where they can pick up room keys. Once in the 1,000-room property, recreation seekers can choose from an indoor pool, health club and tennis courts.

The **Lombard Hilton** is in a strategic location in the Park Terrace Hilton, recently renamed **the St. Louis Airport Hilton** (7060 National Center Rd., St. Louis, MO 63184, 800-445-5500, in Missouri, 800-346-5500). Situated on the site of Lambert International Airport amid 14 acres of landscaped lawns and terraced gardens, the 215 units include the newly redecorated tower guestrooms and the parlor suites—ideal for small gatherings. Along with 20 function rooms and more than 19,000 square feet of meeting space, this Hilton has a complete health club, indoor and outdoor pools, tennis courts, and a championship golf course.

The **Embassy Suites Hotel—Kansas City International Airport** (7640 Northwest Tiffany Springs Pkwy., Kansas City, MO 64154,

800-EMBASSY, in Missouri, 816-891-7788) opens this month in Executive Hills North, a business and residential complex adjacent to the airport and about 25 minutes north of central Kansas City. The 236-unit hostel offers the standard Embassy Suite touches. The guest suites all feature two 25-inch TV sets, two phones, sofa, armchair, wet bar, refrigerator, icemaker, and microwave oven. Guests receive complimentary breakfast and invitations to nightly receptions. And as a reminder that Kansas City is indeed the "City of Fountains," the verdant garden atrium abounds with tiered waterfalls and rippling pools.

Hyatt's very first property was at an airport (LA International), and the **Hyatt Regency DFW** (Box 619014, International Pkwy., Dallas/Fort Worth Airport, TX 75261-9014, 800-233-1234, in Texas, 214-453-8400) is smack-dab in the middle of mammoth Dallas/Fort Worth International. Originally an Amfac Hotel and owned by Hyatt since 1986, the stately twin-towered structure recently underwent a renovation of all 1,380 guestrooms, 93 meeting rooms, and public areas. An in-house Business Communication Center provides secretarial and phone services, private offices, and all the usual high-tech goodies. Guests can enjoy a complete health-and-fitness center and outdoor pool.



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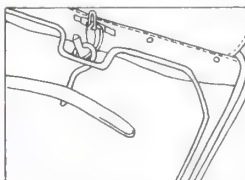
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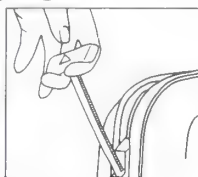
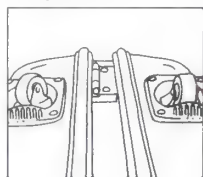
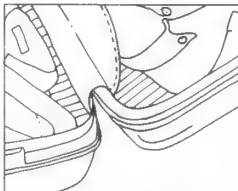
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Well, now that the suit is back in the suitcase, maybe it's time you got back in a luggage store. We bet you'll be surprised just how much our luggage has changed and how much easier traveling can be.


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at the hotel, and five minutes away is the 335-acre Hyatt Bear Creek Golf & Racquet Club with two 18-hole golf courses, seven tennis courts, and ten racquetball courts.

The **Stouffer Concourse Hotel—Denver** (3801 Quebec St., Denver, CO 80207, 800-HOTELS-1, in Colorado, 303-399-7500) excels in convenience. It's three minutes from Stapleton International Airport, ten minutes from Denver proper and the State Capitol complex, and only an hour from the nearest Rocky Mountain ski slopes. Shaped like a gigantic, modern A-frame, the building's slanted walls enclose a bright and cheerful 12-story atrium. All 400 rooms receive such morning perks as wake-up calls followed by complimentary coffee and newspapers, along with access to indoor and outdoor pools, whirlpools, and exercise rooms. The 99 deluxe Club Rooms on the top three floors are treated to a full-service concierge, free continental breakfast, and admission to the Club Lounge for cocktail-hour snacks. The hotel also supplies specialists who—even on short notice—can arrange conference space, airport transfers, room reservations, audiovisual equipment, and anything else necessary for a business gathering.

ONLY IN L.A.

With 1,280 guestrooms and suites and 90,000 square feet of meeting space, the **Los Angeles Airport Hilton and Towers** (5711 West Century Blvd., Los Angeles, CA 90045, 800-HILTONS, in California, 213-410-4000) qualifies as one of the largest airport hotels in the world. A component of the massive Centroplex compound at the entrance to L.A. International, the Hilton just loves taking meetings. Its Pacific Conference Center has an array of rooms that offer sophisticated audio, video, lighting, and sound installations, plus a theater for Hollywood-style screenings. To rise above convention, stay in the 16th- and 17th-floor Towers section, which—like the Hilton's Waldorf Towers in New York—features private check-in, concierge attention, admission to a private lounge, and a well-stocked library.

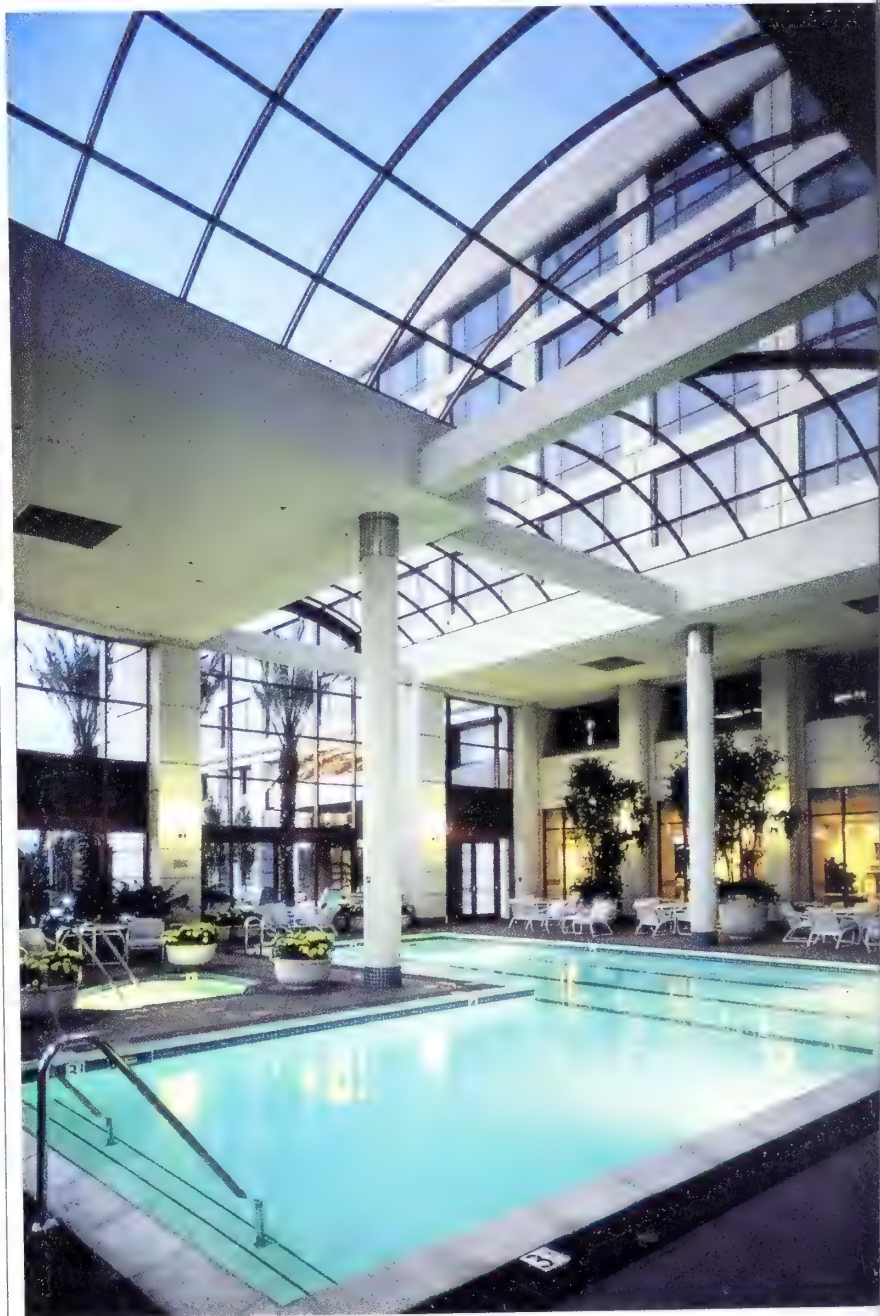
Westin Hotels operates only two airport properties, one of which is the **Westin—San Francisco Airport** (1 Old Bayshore Hwy., Millbrae, CA 94030, 800-228-3000, in California, 415-692-3500). The lobby and other public spaces are decorated in an elegant, understated manner with classic styles of furniture, as are the 393 guestrooms. Recreational activities abound. There's an indoor pool and health club on the premises, and Bay Area shopping and entertainment are nearby. Unlike the rest of the hotel, the *Bayshore Diner* coffee shop is decidedly nontradi-

tional. In a 1950s-style setting with black-and-white checked tiles, long counters, and swivel stools, guests can munch on burgers and keep track of flight schedules via overhead video monitors.

Anchorage may seem remote, but situated roughly equidistant (as the 747 flies) from New York, Tokyo, and northern Europe, it has become a convenient spot for intercontinental conclaves. The **Clarion Hotel—Anchorage** (4800 Spenard Rd., Anchorage, AK

99517-3236, 800-544-0533, in Alaska, 907-243-2300) accommodates such get-togethers with 248 rooms and 6,000 square feet of meeting space located adjacent to Anchorage International Airport on the shore of Lake Spenard, the world's premier floatplane base. For globe-trotters yearning to get physical, there's an ice-skating rink during the lengthy Alaskan winter, a jogging and cycling trail when the snow melts, and a health club with a sauna all year long.

In the swim: the pool at the Westin-San Francisco Airport.





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TRAVELER

THE TRAVELING PHOTOGRAPHER

LESS IS MORE
WITH THE NEW LENS-SHUTTER COMPACTS

Every executive knows what a picture's worth, but it used to seem that writing those proverbial thousand words back at the office was faster and easier than getting a good, sharp photograph on a business (or pleasure) trip.

The dilemma: Small, simple cameras (like the disk models in vogue a few years ago) relied on tiny film formats that compromised image quality, while the increased clarity possible with 35mm film meant resorting to large and relatively complicated single-lens reflex (SLR) cameras. Recently, however, a new breed of camera has evolved that combines point-and-shoot simplicity with SLR quality—and all in a package that slips easily into a purse, pocket, or briefcase.

The lens-shutter compacts, as they're known, simplify 35mm photography by offering a host of automatic functions that take care of focusing, exposure, flash, film-speed setting, film loading, and film transport. But this streamlining doesn't come at the expense of creative flexibility. For all their convenience, these cameras are serious picture-taking instruments, representing a blend of innovation and tradition. In fact, many sophisticated features pioneered in compact 35mms—such as ergonomic design and easier film loading—have begun to be adopted by their SLR cousins.

THREE WAYS TO GO

There are three sorts of pocket-size lens-shutter cameras. Single-focal-length models, equipped with a wide-angle lens (about 35mm) for standard shots, dual-focal-length compacts, which add a switchable telephoto lens element (around 70mm) to bring the action closer, and autofocus zoom cameras for continuous coverage throughout the range from wide angle to telephoto. Among the newest generation there are even models with computerized "databack" modules that permit photographers to imprint dates or other information directly on the film.

The most significant considerations in choosing a camera are personal. Having a clear idea of how it will be used—whether indoors or out, for close-ups or panoramas,

portraits or action shots—is no less important than a quick hands-on examination to determine the layout of the controls and how the camera feels. Because all the cameras described here are designed to fill the same niche, the seemingly minor differences between them become major. For example, not all compacts using the DX encoding system to set the correct film speed automatically are equal (the camera does this by reading the bar code that appears on almost all 35mm slide- and print-film cartridges). Some models are more limited in the range of speeds they accept than others. Using a relatively slow slide film—such as the popular Kodachrome 25 or Fujichrome 50—in a camera that can't accommodate it will result in improperly exposed photos. Photographers partial to a particular type of film should check the specifications of any camera they're thinking of buying to avoid disappointment.

SINGLE-FOCAL-LENGTH COMPACTS

All of these models offer autofocus, automatic exposure through a range of continuously set shutter speeds, film-speed setting, motorized film advance between shots, integrated flash, and a built-in lens shield as standard equipment. Almost all feature fast f/2.8 or f/3.5 lenses, automatic film rewind, and fill-flash (which adds just enough light to illuminate the subject in contrasty shots without washing out the background). And several are powered by lithium batteries, which permit flash recycling in as little as one second.

The **Canon** Sure Shot Supreme (\$328) has the flowing, organic lines fast becoming a company trademark, a useful liquid crystal display (LCD) panel that keeps track of shots taken, and a lithium power source. The Sure Shot Supreme Quartz Date databack version lists for \$364.

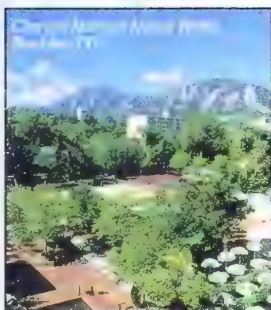
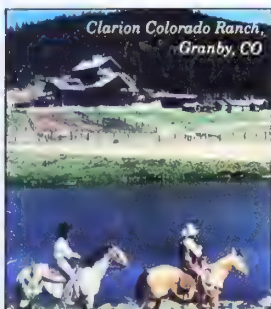
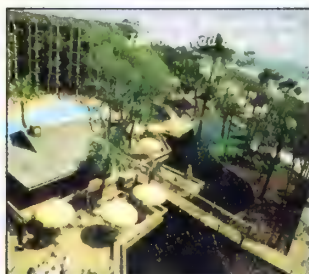
Fuji's compact features an ingenious Drop-In autoload system designed to make film loading no harder than putting a cassette into a tape player. The "back to basics" approach taken by the DL-120 (\$149.95) will suit novices, while more advanced photogra-

phers will appreciate the DL-300's (\$245.95) manual overrides and its large LCD readout window, which helps to monitor camera functions.

Kodak, a name synonymous with photography, resumed making 35mm cameras in 1986, after a 16-year hiatus. Their brand-new S1100XL (\$179.95) is a rugged unit with the flash housed in its distinctive flip-up lens cover—a position designed to minimize the "red eye" effect.

The shutter release and other controls found on **Minolta's** trim Freedom III (\$282





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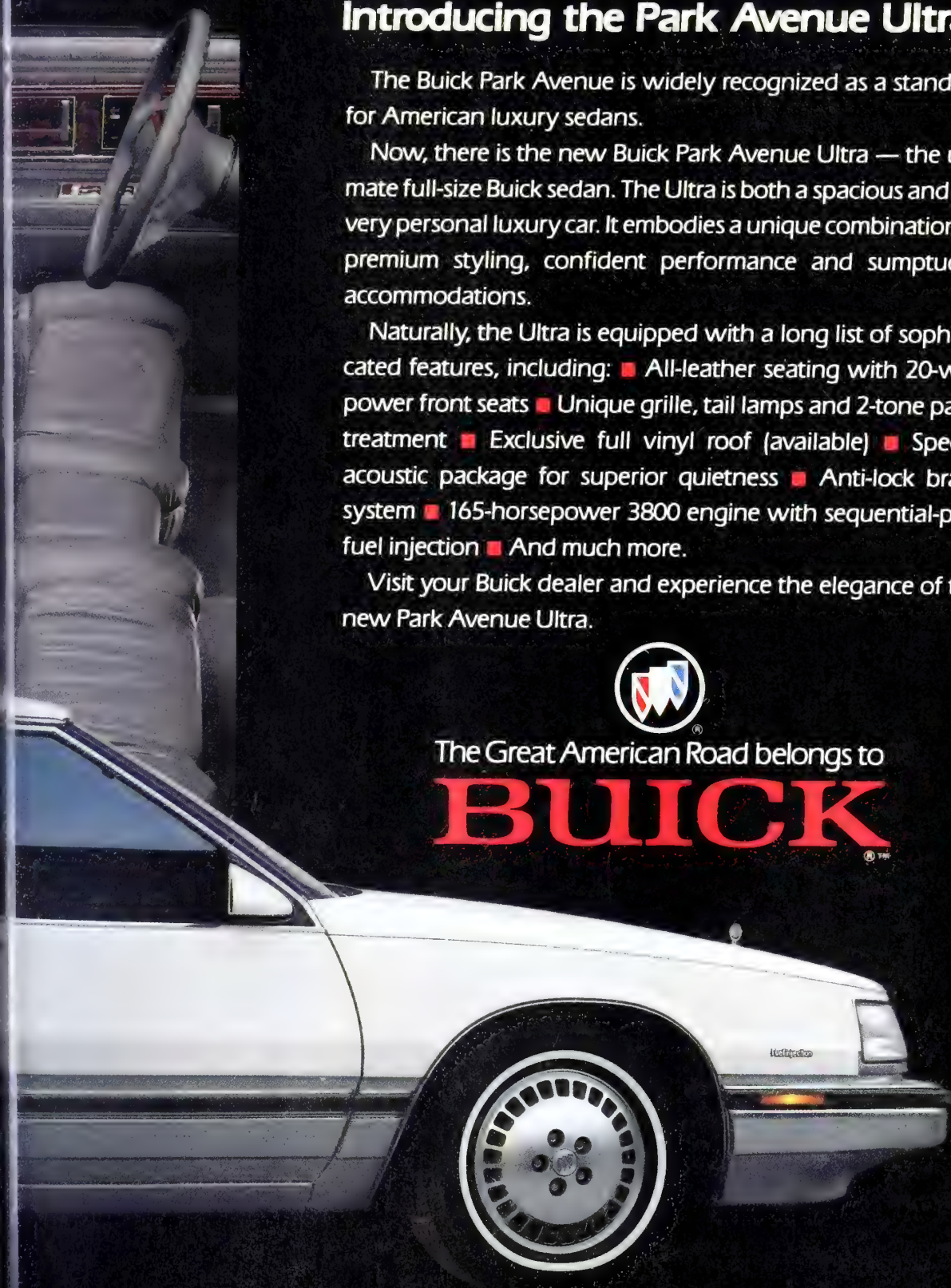
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are high-tech, pressure-sensitive pads rather than conventional mechanical buttons. In addition, the Freedom III employs a version of the five-beam autofocus system pioneered in the company's ground-breaking Maxxum SLRs. There's also the option of using either a lithium power source or traditional alkaline batteries.

Need a camera to capture those underwater business meetings with Jacques Cousteau? Nikon's aptly named Action-Touch (\$322) is an all-weather model that's at home above and below the sea. Fully automatic on dry land (where its system of seals protects against sand or rain), it also offers the manual control of focusing and flash necessary when submerged in depths of up to ten feet. And for the adventurous but landlocked picture-taker, the Nikon One-Touch's (\$275) macro-focusing capability lets users get as close as 18 inches to their subject.

The Olympus Infinity Jr (\$219) is a compact's compact—weighing just over seven ounces and only slightly bulkier than a cigarette pack—that doesn't sacrifice features for size. A fraction larger is the Infinity itself (\$305), which adds a faster lens with aspheric elements, water resistance (but not submersibility), and fill-flash.

Ricoh packs several surprises into another camera about the same size as the Infinity siblings. The distinctive FF-7 (\$250, databack version, \$287) uses an LCD window to keep track of its five special modes for shooting landscapes, available-light night shots, TV screens, continuous sequences of up to one frame per second, and automatic shots at one-minute intervals.

One of the most exciting innovations in the compact field is found on the Yashica T3

(\$375). An auxiliary top-mounted viewfinder, alongside the LCD readout, allows photographers to frame a shot without lifting the camera to eye level—perfect for capturing action unobtrusively.

DUAL-FOCAL-LENGTH COMPACTS

For those who want to cut down the distance between camera and subjects, these models feature a telephoto option along with the normal wide-angle view—just change the setting from standard to tele and faraway objects are magnified up to two times. Although these cameras are slightly bigger to accommodate the additional optics, they share all the standard automatic elements of single-focal-length compacts.

Besides offering 35mm and 60mm lengths, Canon's outstandingly sleek Sure Shot Multi Tele (\$399) can be set to take vertically oriented half-frame exposures, thereby doubling the number of shots per roll. An optional external teleconverter boosts the upper focal length to 75mm.

Fuji equips its DL-400 Tele (\$349.95) with 35mm and 70mm focal lengths and complements its Drop-In loading with an unusual film prewind system. When the camera back is closed, the entire roll is drawn out of the film cartridge and wound around the take-up spool. Each exposure is then pulled back into the cartridge as it's shot, eliminating rewinding after the last picture and protecting exposed film from light if the camera is accidentally opened in midroll.

Minolta's Freedom Tele (\$385) lets users choose either a 38mm or 80mm focal length and can focus down to 28 inches. An optional teleconverter increases the range to 105mm.

The Tele-Touch Deluxe (\$372) from Nikon lives up to its manufacturer's reputation for innovation by squeezing 35mm and 70mm focal lengths into a body almost the same size as the One-Touch—without sacrificing sophisticated automatic functions.

The Olympus Infinity Twin (\$325) solves the wide-angle/tele engineering problem in a novel way. While most dual-focal-length compacts are equipped with only one lens (which is used together with internal optical elements for magnification), the Twin sports two separate autofocus lenses: a 35mm and a 70mm mounted below. This independent lens design maximizes the Twin's optical performance and also results in a compact that's exactly that.

The controls and LCD window on Ricoh's TF-500 (\$351) are handily clustered on the camera's top panel. It can shoot in either single-frame or continuous-sequence modes, and with an accessory converter its

70mm focal length can be increased to 105mm.

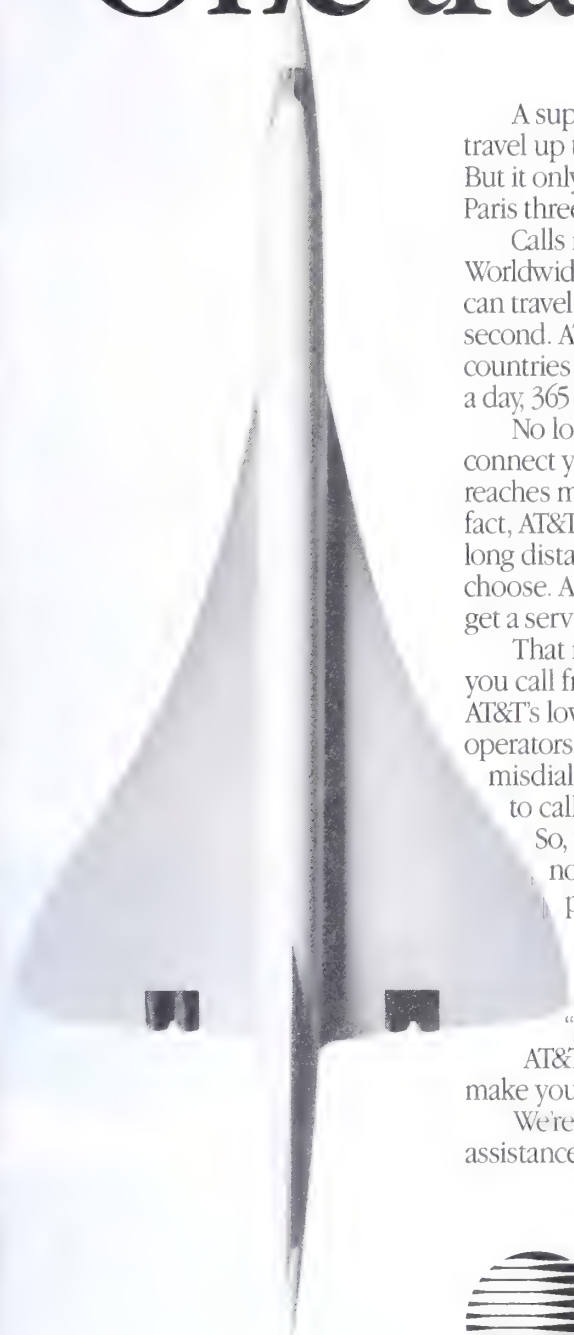
AUTOFOCUS ZOOM COMPACTS

This category of camera represents the ultimate for photographers who want to get "up close and personal" without lugging a bagful of equipment along. Closest in size and styling to SLRs, these compacts are outfitted with lenses that barrel in and out of the camera body to let the user determine the exact framing of each shot. Their viewfinders and flash units work in tandem with the lens, ensuring an accurate image of the shot and guaranteeing the proper illumination for the focal length chosen. And all utilize LCD panels to monitor camera status.

Canon's Sure Shot Zoom (\$459) has a surprise in store for camera buffs who've come to expect push buttons to do all the work. Although other functions are automatic, the 35–70mm zoom lens is manual. Why? Zooming by hand is preferred by many veteran photographers, who feel that it affords more control and speed than some motorized systems. And without an extra motor on board,



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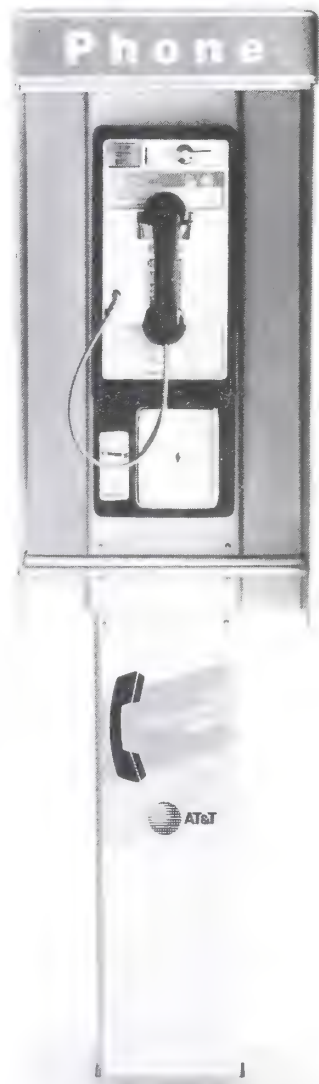
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battery life is extended
 Fuji's current top-of-the-line compact zoom, the 35-70mm Discovery 500 Zoom (\$399.95), will lose its pride of place when the

FREQUENT TRAVELER

company's Discovery 2000 Zoom (\$519.95) hits camera stores this summer. The new model promises to outshine its predecessor with a remarkable 40-105mm powered zoom, continuous shooting for rapid sequences, and an advanced flash system that accepts a powerful, auxiliary dedicated flash unit.

The brand-new Freedom Zoom 90 (\$428) is Minolta's first entry in the compact-zoom field. When the generous 38-90mm zoom range is augmented by an optional extender

(which provides coverage of up to 120mm), this camera offers the greatest focal-length range available for its size.

Slightly more than two inches thick, the Nikon Zoom-Touch 500 (\$404; databack version, \$420) is the thinnest compact zoom around (thanks to a two-stage retracting lens barrel), yet it covers an impressive 35-80mm range. Sports and action photography are a snap because of automatic-sequence zoom shooting, which takes three shots in a row at 35mm, 53mm, and 80mm. Five preset zoom lengths—from wide to tele—are also available at the touch of a button.

The powered 35-70mm lens on the Olympus Quick Shooter Zoom (\$440) is controlled by an ingenious dial right under the user's thumb. This is a camera designed to nurture the creative impulses of even casual users with its wealth of options, including four different flash modes, macro-focusing, multiple-exposure capability, and compatibility with special-effects filters.

The **Pentax IQZoom 60** (\$324, databack version, \$359) handily incorporates its shutter button on the same triangular switch that controls the motor of the 38-60mm lens, making it easy to frame and then shoot with just the slightest shift of a finger. More advanced picture-takers should check out the fully equipped **IQZoom 70** (\$437; databack version, \$489), which has a 35-70mm range that can be increased to 100mm with a teleconverter.

Vivitar's two compact zooms, the 300Z (\$289.95) and the TEC 155 (\$399.95), both employ manual zooming. With a 38-60mm lens and a minimum of control buttons, the simplicity of the 300Z makes it a good introduction to zoom cameras. The more sophisticated TEC 155 offers manual overrides for its automatic functions, a 35-70mm lens, and a top-mounted dial indicating the selected focal length.



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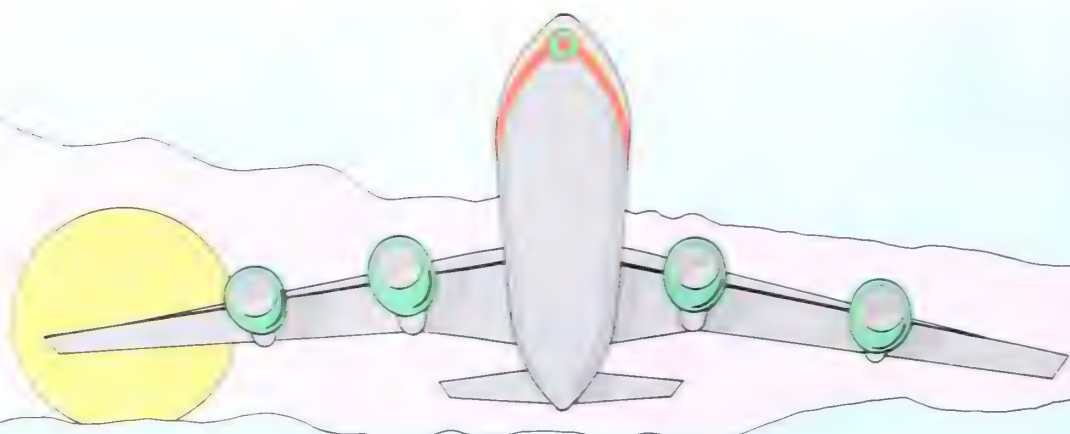


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FREQUENT
TRAVELERTHE AIRLINES
OF ASIAA GUIDE TO THE MAJOR CARRIERS
THAT ENABLE EAST TO MEET WEST

In the past few years, airlines from Asia have been making a big splash in the U.S. market. In 1990, for example, United, Northwest, Delta, and American Airlines all had new Asian routes. And in 1991, Japan's All Nippon Airways (ANA) and Korean Air will both launch new U.S. routes.

HOW MANY I SERVE YOU?

When it comes to the number of seats on a plane, the airlines of Asia are in a bit of a race. ANA's new 747-300, for example, will have 366 seats in its main cabin. That's more than Delta's 747-300, which will have 364 seats. And ANA's new 747-300 will have 366 seats in its main cabin, which is more than Delta's 747-300, which will have 364 seats.

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CELESTIAL CUISINE

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and Singapore Airlines has 18 from Los Angeles to Singapore. Cathay Pacific's dedication to the art of good service earned it 1987's Airline of the Year award from *Air Transport World*, an industry publication.

Besides service, passengers are lured by frequent-flyer benefits. Several Asian airlines—among them All Nippon, JAL, Korean Air, Philippine, and Thai—will credit a corporate mileage account so that a company footing the bill (along with the employee who is traveling) can earn free tickets and upgrades.

GROWING COMPETITION

Because air travel in Asia has become a highly competitive proposition (growing at a double-digit rate, thanks to the region's rapidly expanding economies and increased tourism), an ever-increasing number of North American carriers have joined the fray. United, Northwest, American, Delta, Continental, Air Canada, and Canadian compete zealously on the frequent-flyer battlefield. The numerous mileage points that can be accrued on transpacific flights are often an important consideration for travelers who

use those carriers to connect with non-gateway American cities.

According to industry analysts, the upswing in Asian air traffic is expected to continue throughout the 1990s, with international air travel providing the impetus for this expansion. Business for Asian airlines is increasing within the region as well, especially in Thailand, Hong Kong, Taiwan, Singapore, and Japan. In Taiwan, for example, many of the travel restrictions that were placed on its citizens have been lifted, making for more crowded flights. The new Sino-British agreement on Hong Kong has helped spur air traffic there, too. Cathay was originally a British airline, sharing its operating rights with British Airways and other U.K. carriers. Now it runs four L-1011 flights per week between Hong Kong and Shanghai, and two L-1011 trips a week between Hong Kong and Beijing.

There is still, however, an imbalance with CAAC (China's flag airline), which has about twice as many flights in the Hong Kong-Shanghai market and three times as many in the Beijing market. Airline experts believe this will change in the not-so-distant future,

as Hong Kong becomes the regional headquarters for more international corporations. It's now home to 155 banks and is the major financial center that stays open while New York and London sleep. Travelers headed there are advised to book as far ahead as possible.

Indeed, as the major Asian cities become more important to world commerce, so do their airlines and airports. Bangkok International Airport, home of Thai Airways, has recently increased facilities for international check-in, baggage handling, and immigration, thereby making the airport one of the four main East Asia hubs, along with Singapore, Hong Kong, and Tokyo. There's talk of building a second airport in Bangkok and in Hong Kong, and Changi Airport in Singapore will expand its facilities considerably when Terminal Two opens in early 1990. The addition will feature state-of-the-art airport technology.

The following chart lists the Asian airlines with the most extensive service to the United States, along with their major routes, special amenities, frequent-flyer tie-in programs and seating arrangements.

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All Nippon Airways Tokyo, Japan	29 major cities in Japan, China, the South Pacific, and North America	Los Angeles and Washington, D.C.	Own program, including corporate credits
Cathay Pacific Airways Hong Kong	35 major cities in 24 countries on 4 continents	San Francisco and Vancouver	Own program plus American
China Airlines (CAAC) Taipei, Taiwan	19 major cities spanning 3 continents	Honolulu, Los Angeles, New York, and San Francisco	Own program
Garuda Indonesia Airways Jakarta, Indonesia	35 cities in Indonesia, 5 cities in Australia, 2 cities in the United States, 7 cities in Europe, plus New Zealand, Tokyo, Taipei, Manila, Singapore, Kuala Lumpur, Penang, and Bangkok	Honolulu and Los Angeles	USAir and Eastern
Japan Air Lines (JAL) Tokyo, Japan	59 cities in 33 countries on 6 continents	Anchorage, Atlanta, Chicago, Honolulu, Los Angeles, Mexico City, New York, San Francisco, Seattle, and Vancouver	Own program plus Delta and TWA along with a corporate passbook gives awards to companies
Korean Air Seoul, South Korea	36 destinations throughout Africa, Asia, Europe, and North America	Honolulu, Los Angeles, New York, Toronto, and Vancouver	Own program, including corporate credits
Malaysia Airline Kuala Lumpur, Malaysia	More than 60 destinations in 21 countries spanning Europe, the Middle East, and Asia, along with Australia and the United States	Honolulu and Los Angeles	Eastern
Philippine Airlines Manila, Philippines	32 cities in 23 countries linking Asia, Australia, Europe, the Middle East, and the United States	Honolulu, Los Angeles, and San Francisco	Own program, including corporate credits, plus USAir
Qantas Airways Sydney, Australia	42 cities in 20 countries in Africa, Asia, Australia, Europe, North America, and South America	Los Angeles, San Francisco, and Vancouver	Own program plus American
Singapore Airlines Singapore	57 cities in 37 countries across 5 continents	Honolulu, Los Angeles, San Francisco, and Vancouver	Own program plus American
Thai Airways International Bangkok, Thailand	50 cities in 37 countries in Africa, Asia, Australia, Europe, and North America	Dallas/Fort Worth, Seattle, and Toronto	Own program, including corporate credits, plus Alaska Airlines



NG

1st class seats, 60-inch seat pitch, 2 x 2 configuration; 56 pacific class 40-inch seat pitch, 2 x 4 x 2 configuration

1st class seats, 60-inch seat pitch, 2 x 2 configuration; 80 business seats, 40-inch seat pitch, 2 x 2 x 2 configuration

1st class seats, 56-inch seat pitch, 2 x 2 configuration; 40 Marco Polo class seats, 38-inch seat pitch, 2 x 2 configuration

1st class seats, 62-inch seat pitch, 2 x 2 configuration; 66 dynasty class seats, 40-inch seat pitch, 2 x 2 x 2 configuration

1st class seats, 57-inch seat pitch, 2 x 2 x 2 configuration; 24 executive class seats, 42-inch seat pitch, 2 x 2 x 2 configuration

14 first class seats, depending on aircraft, 60-inch seat pitch, 2 x 2 configuration; 94 to 164 executive class seats, depending on aircraft, 36-inch seat pitch, 2 x 4 x 2 configuration

8 first class seats, depending on aircraft, 60- to 62-inch seat pitch, configuration; 24 to 40 prestige class seats, depending on aircraft, 38-inch seat pitch, 2 x 2 configuration

7 first class seats, 60-inch seat pitch, 2 x 2 configuration; 30 to 38 club class seats, depending on aircraft, 42-inch seat pitch, 2 x 2 x 2 configuration

10 first class seats, depending on aircraft, 41-inch seat pitch, 2 x 2 configuration; 34 to 40 mabuhay (business) class seats, depending on aircraft, 37-inch seat pitch, 2 x 4 x 2 configuration

8 first class seats, depending on aircraft, 60-inch seat pitch, 2 x 2 configuration; 16 to 66 business class seats, depending on aircraft, 38-inch seat pitch, 2 x 4 x 2 configuration

1st class seats, 60-inch seat pitch, 2 x 2 configuration; 56 business seats, 37- to 38-inch seat pitch, 2 x 2 configuration

8 royal first class seats, depending on aircraft, 60-inch seat pitch, configuration; 42 to 62 royal executive class seats, depending on aircraft, 42-inch seat pitch, 2 x 2 configuration

AMENITIES

Advance seat selection; separate check-in; priority baggage; priority boarding; separate departure lounge; toiletry/shaving kit; assorted other gifts; lamb's-wool seat covers; complimentary cabin bag

"Classroom in the Sky," an in-flight language lab designed to teach Japanese to English speakers; separate check-in; priority baggage; priority boarding; guidebook to Tokyo; toiletry/shaving kit; reservation service for All Nippon Airways (ANA) hotels

Advance seat selection; separate departure lounge; priority baggage; priority boarding; footrests in business class; toiletry/shaving kit

Advance seat selection; express computerized check-in; doorside loading; priority baggage; priority boarding; separate departure lounges; toiletry/shaving kit; other assorted gifts; only carrier with international flights serving Tokyo's nearby Haneda Airport

Special check-in; priority baggage; priority boarding; free drinks, including champagne

Advance seat selection; separate check-in; priority baggage; priority boarding; separate departure lounge; toiletry/shaving kit; happi coats and slippers; Japanese/English and Chinese/English name-card service; reservation service for Japan's bullet train; special check-in and check-out services and room rates at selected hotels throughout Japan; hospitality desks at most hotels; room-and-rail packages for independent train travel; access to Executive Service lounge at the Imperial Hotel in Tokyo; gift services

Advance seat selection; separate check-in; priority baggage; priority boarding; gifts in-flight such as calculators, stationery, and fresh ginseng (to fight fatigue) for first-class passengers; recent improvements of facilities at Seoul's Kimpo Airport

Separate check-in; priority baggage; priority boarding; shaving kits; complimentary gift: duty-free shopping on board; private airport lounges in Malaysia and 16 cities worldwide; if layover in Subang Kuala Lumpur International Airport is 2½ to 6 hours, a complimentary room at Subang Airport hotel is provided

Advance seat selection; separate check-in; priority baggage; priority boarding; separate departure lounge; Skybed in first class; toiletry/shaving kit; duty-free shopping in-flight; complimentary gift

Advance seat selection; separate check-in; priority baggage; priority boarding; escort service; toiletry/shaving kits

Advance seat selection; smoke-free upper decks; separate check-in; priority baggage; priority boarding; complimentary gift; worldwide emergency-assistance program; private departure lounges in major airports

Advance seat selection; separate check-in; priority baggage; priority boarding; separate departure lounge; shaving kits and other gifts; upper deck reserved for nonsmokers; private bar facilities; automatic upgrades when connecting to American, Alaska, Continental, or Delta; fresh orchid corsages; meet-and-assist program; comfort socks

A suite at the Mondrian as interpreted by Italo Scanga, Los Angeles, 1989



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**FREQUENT
TRAVELER**

PURCHASE PROTECTION: SHOULD YOU LEAVE HOME WITHOUT IT?

PROBABLY NOT, BUT READ THE FINE PRINT FIRST

Scene 1 The vase is so expensive, but absolutely gorgeous "We'll take it," the handsome young couple decides. An American Express card materializes.

Scene 2 Back home, the vase topples off the refrigerator and smashes into smithereens. A total loss—until the husband recalls some sort of American Express insurance deal. He reaches for the phone.

Scene 3 A new gorgeous vase implanted in a new location. Smiles all around. The end.

The commercial touts the restorative powers of Purchase Protection, a no-cost provision of American Express that promises to replace, repair, or compensate cardholders for damage, loss, or theft of most any item purchased with the card. Introduced in 1987, Amex's program has since prompted the bankcards to offer similar programs for gold and even some regular cardholders. Visa calls its version Purchase Security, and MasterCard, Purchase Assurance.

Are these "buyer protection" programs the consumer breakthrough they seem? Yes, sort of. They can deliver what they promise, but because the plans contain a fair amount of fine print and settlement involves a good deal of red tape, consumers dreaming of the painless restitution depicted in the commercials are in for a rude awakening.

TOO GOOD TO BE TRUE?

The buyer protection programs of the Big Three are virtually identical. All feature up to \$50,000 of insurance per cardholder against any loss, whether due to theft, accident, or fire. Coverage applies to purchases made with the credit or charge card anywhere in the world for 90 days from the date of purchase—not long, but possibly long enough to prevent the utter devastation of losing an item not yet paid for. Coverage goes into effect automatically; no registration is required.



Once a claim is made (form submitted, documentation furnished), claimants should receive compensation in five days to two weeks. American Express members and Visa Gold and Gold MasterCard carriers pay nothing extra to participate in the program. (All three companies also offer separate but related programs that double the life of warranty periods up to an extra year for merchandise purchased within the United States.)

That's the good news. Now for the fine

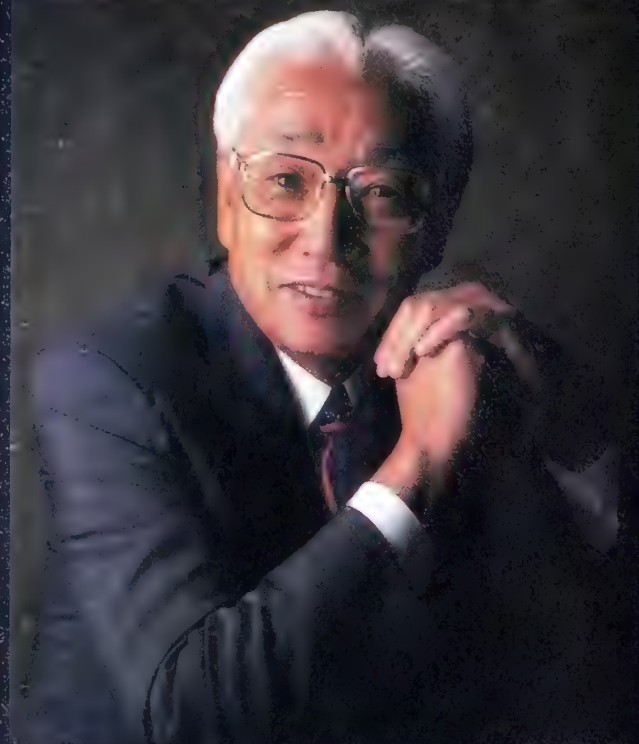
print: Coverage applies *only in excess of other collectible insurance*. Oh, there are the usual insurance-ese disclaimers that exclude compensation in cases of fraud, abuse, floods, earthquakes, wars, radioactive contamination, inherent product defects, or mysterious disappearance. And coverage does not apply to cash, traveler's checks, tickets, "negotiable instruments" (bonds, stock certificates), living plants and animals, or jewelry from baggage, unless carried by hand by the cardholder or someone known previously by the cardholder. Gifts charged to the card are covered only when given to members of the household who have the same permanent address as the cardholder. But before you call the toll-free hot line, outline your case, and wait for the claim form to arrive in the mail, consider whether you may already be covered under an existing policy. You could be in for a lot of work.

I'D RATHER FILL OUT TEN 1040s

"Your claim must always be submitted initially to your homeowners insurance carrier, renters insurance carrier, personal property insurance carrier, motor vehicle insurance carrier, business liability insurance carrier, fire insurance carrier, or to the liability insurance carrier of anyone causing you loss, and, in the case may be, prior to submitting the Loss Report," reads the preface to the four-page American Express claim form.

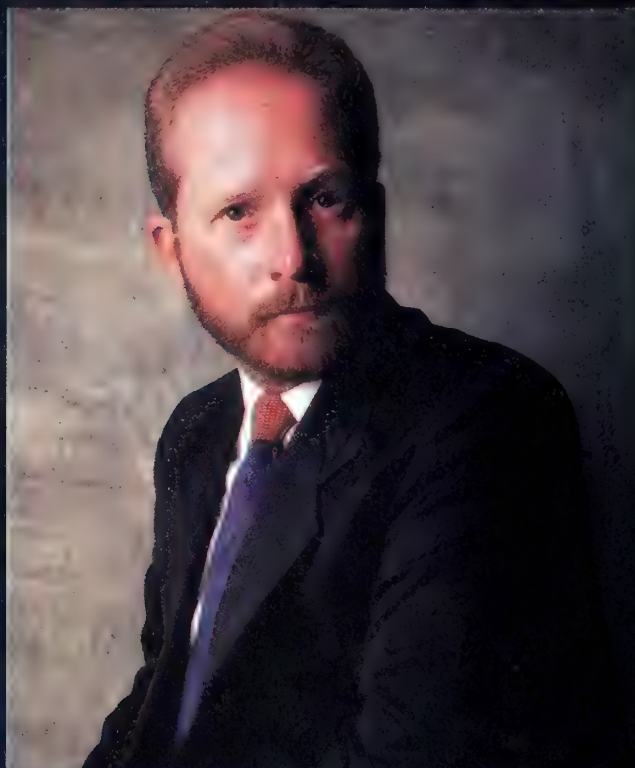
The report itself provides spaces for the names of the companies that insure you in each of those areas and your policy number. For each type of insurance you must check off a "yes" or "no" to the question, "Was the claim/loss submitted to your... carrier?" and in each case are reminded, "If yes, submit legible copy of this claim submission. If no, and if applicable, please file such a claim before submitting this loss form."

Why JAL?



"I like organizations that pay attention to details. I feel at home."

Akio Morita
Chairman of the Board &
Chief Executive Officer
Sony Corporation
Tokyo, Japan



"I respect an operation when it's managed by true professionals."

Jeffrey A. Barks
Associate Dean for Master's
and Bachelor's Programs
Sloan School of Management
M.I.T.

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FREQUENT TRAVELER

How likely is it that insurance you already carry will apply? Very likely, especially if you own a home. According to the Insurance Information Institution, a nonprofit trade organization representing 300 property and casualty companies, 95% of homeowners carry homeowners policies that usually cover both at-home calamities and losses suffered outside the home. Renters typically have the greatest need for buyer protection. With many assuming (erroneously, in most cases) that the landlord's insurance covers their personal property, only 23% of renters carry a relatively inexpensive (generally \$125 to \$175 a year) renters policy.

However, both homeowners and renters policies have deductibles that range from \$100 to \$500, with \$200 or \$250 currently the most common amounts. What buyer protection can do is "fund the deductible," and,

together with existing personal insurance, cover 100% of larger losses. If, for example, your homeowners policy has a \$250 deductible and you lose a \$1,500 watch, you get \$1,250 from your insurance company and \$250 from buyer protection. Homeowners or renters insurance wouldn't cover a ruined \$100 sweater, but Amex/Visa/MasterCard should cover the full amount. Buyer protection also covers losses or damages that fall below the deductible on a primary policy. And, unless you've taken an extra-cost personal articles floater, you may need buyer protection to cover the full value of expensive items like furs and jewelry.

NO QUESTIONS ASKED?

When substantiating claims, card companies mimic the "Trust, but verify" approach, and insist that claimants provide

any and all relevant documentation: sale receipts, charge slips, police or fire reports, if applicable; names, addresses, and phone numbers of witnesses, estimates and insurance policies. If an item is damaged, you may have to send it to a claim office to assess damage (sometimes a photo will suffice) and then determine whether to repair or replace.

What happens in the event of an accidental, nonverifiable, total loss like the one depicted in the commercial? "If something is broken beyond repair, we won't make them send us the pieces," says James M. Erlich, vice-president of American Express Cardmember Services. "There are certain built-in fraud checks that obviously I can't talk about. But from our own independent inspection and analyses we've found a very minimal amount of what we could call 'questionable behavior.'"

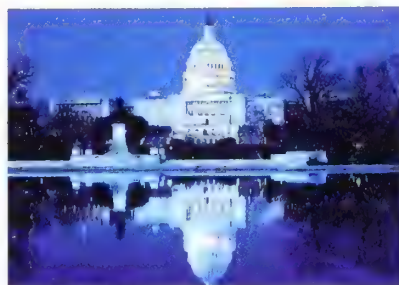
Differences between the provisions of the Big Three's programs are minuscule. Visa and MasterCard have 24-hour, seven-day claim hot lines; American Express is available on weekdays between 9 A.M. and 8 P.M. Eastern time. Visa Purchase Security may be available to nongold cardholders. At this point, Visa and MasterCard will cover items purchased through October 31, 1989, the current American Express program expires May 31, 1989, and at press time the company was noncommittal about its future.

TIME IS MONEY

As comprehensive as the system sounds, it doesn't necessarily work for everybody. Alexandra Mayes Birnbaum, wife of the editor of this section, had to call American Express three times just to obtain a Loss Report after an expensive new suitcase was damaged during a trip home from Hong Kong. At first Amex insisted that she ship the yard-wide suitcase to Denver, but they eventually allowed a Polaroid picture of the damage to suffice. When the Birnbaums finally received the application and understood what would be required to make the claim, they decided it was far more cost- and time-effective to pay a local repair shop \$40 and have the job done themselves.

Indeed, for small losses, the hassles of filing claims may make these schemes more trouble than they're worth. Insurance is like that. But for larger claims, and particularly those that may fall between the cracks of other coverage you may carry, this no-coverage program may represent the only way to avoid total loss. Stated in contemporary political terms, buyer protection provides a temporary "safety net" to stave off utter disaster; it does not offer the "kinder, gentler" protection the advertising may lead you to expect.





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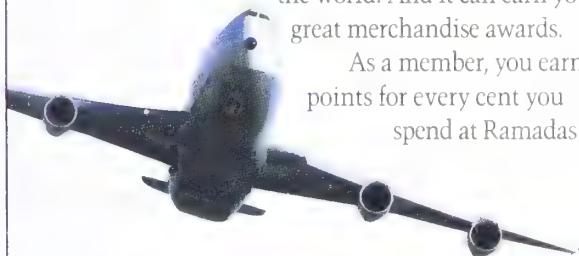
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FREQUENT TRAVELER

BRUNCHING IT

THE PICK OF THE CROP FOR WEEKEND DINING
IN CITIES ACROSS AMERICA



Southern graciousness and plenty of grits set the tone at Rogers Barbecue in Charlotte

Whether by design or default, many business travelers often find themselves spending the weekend in an unfamiliar city. One way in which to shed the corporate image and feel like a native (if only for a few hours) is to seek out a pleasant brunch spot. We don't mean donning the suit and tie and taking the elevator down to the hotel dining room for such standard buffet fare as warmed-over eggs Benedict or (yawn) smoked salmon and cream cheese on a bagel.

We're talking about leaving that whole hotel scene behind, about getting out and exploring the city until you find a terrific brunch place, which can be anything from an elegant, upscale eatery to an unadorned café. The essential ingredients are great food and a relaxed atmosphere in which to read the paper and sip a second cup of coffee. The following establishments in hub cities across the country run the gamut from high-tech style to down-home quirkiness, but what they all do wonderfully well is serve sensational midday meals on Saturdays and/or Sundays.

ATLANTA Chef's Café

This is the sort of civilized, low-key place where a solitary bruncher can sit reading for hours without being disturbed by other patrons or the staff. The bright, airy space has modern furniture and a rotating selection of artwork on the walls; one nice detail is the sheets of white paper over the linen tablecloths, which often inspire diners' creative impulses. The extensive menu includes the de rigueur omelets and pancakes, along with more exotic offerings such as crab cake Benedict and southwestern frittata (an open-faced omelet with cheddar cheese, black-bean salsa, and sour cream). There's an impressive wine list, with many selections available by the glass. Open Sundays only, 10 A.M. to 2:30 P.M. (2115 Piedmont Rd. N.E., 404-872-2284).

CHARLOTTE Rogers Barbecue

As all southerners know, heaven is a place where breakfast can mean but one thing:

scrambled eggs dished up with sausage gravy, grits, hash browns, and homemade biscuits. The folks at Rogers sure know that, and they've been preparing such traditional country breakfasts since 1935. Don't expect any glitz or glitter here—just plain and simple southern comfort. For more adventurous culinary souls, Rogers's specialties are, I guess what?—barbecue (chopped whole hog, North Carolina-style) and Brunswick stew, both served with coleslaw and cornbread or hush puppies. One of the last great bargains around is the 15¢ "bottomless" cup of coffee, which, according to the menu, comes in either "regular or unleaded." Open Saturdays and Sundays from 6 A.M. to 1 P.M. (901-H North Wendover Rd., 704-364-2939).

CHICAGO Ann Sather's Restaurants

The original of these two eateries may be the only Swedish restaurant in the world that's housed in a former funeral home. Located on West Belmont Avenue in the Lakeview area, the main Ann Sather—a Chicago institution—is near some of the city's

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OF FLYING**



AIR FRANCE

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Air France Executive Europe program valid throughout 1989.

FREQUENT TRAVELER



and pastries for the restaurant. Open for brunch on Sundays only, 11 A.M. to 2:30 P.M. (2515 McKinney Ave., at Fairmount, 214-871-7373)

DENVER

Pour la France Cafés

The first of these bistrolike restaurants appeared in Aspen eight years ago, and its fame has spawned one sister establishment in Boulder and two in Denver. Recommended by both *Gourmet* and *Food & Wine* magazines, Pour la France Cafés are comfortable, casual, and the perfect setting for a laid-back weekend brunch. The menu selections are fresh and filling, representing a blend of American and French cooking. Grand Marnier french toast garnished with bananas and strawberries, shrimp-and-crabmeat quiche, and eggs Arnold (poached eggs on a butter croissant with avocado and hollandaise sauce). All the cafés have bakeries, which have been praised to the skies for their endless dessert offerings. Open Saturdays and Sundays from 8 A.M. to 2 P.M. (730 South University Blvd. 303-744-1888, and 8101 East Belleview Ave. 303-220-8820)

finest theaters (such as Steppenwolf) and only four blocks from Wrigley Field. All traces of the building's previous occupants are gone, replaced by a Scandinavian café with warm mahogany paneling in the front area and a funky diner in the rear. The food ranges from time-honored Swedish dishes to hearty American fare. Swedish pancakes with lingonberry syrup, pork-sausage patties and rich country gravy, and beefsteak and eggs with Ann Sather's legendary cinnamon rolls. Open all day Saturdays and Sundays from 7 A.M. (929 West Belmont Ave., 312-348-2378, and 5207 North Clark St., 312-271-6677)

DALLAS/FORT WORTH

San Simeon

Situated on the outskirts of downtown Dallas, this has become one of the city's leading restaurants since it opened in 1986. The elegant interior features terrazzo floors, arched ceilings, wrought-iron fixtures, and mirrored walls. The menu of innovative American cuisine changes seasonally, and because it offers only the freshest ingredients available, the kitchen was built without a freezer. Among the brunch appetizers might be a banana-macadamia waffle with apricot syrup and herb sausage or smoked pheasant with goat cheese and a white bean tostada. Entrées could include smoked tenderloin of pork and apple-bacon pancakes with maple-sage sauce, and Alaskan-salmon-and-spinach croquettes with three-cabbage coleslaw. San Simeon's neighboring bakery Petaluma, prepares freshly baked desserts



The first of Chicago's two Ann Sather's restaurants (top, left) is probably the only Swedish eatery in the world that occupies a former funeral home. An elegant entrance beckons at San Simeon in Dallas (left).



Suit pressed with a button
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FREQUENT TRAVELER



Denver's Pour la France Cafés (left) are the essence of Colorado cool; the inviting outdoor courtyard at Brennan's in Houston (below).

HOUSTON

Brennan's

The proprietors of this restaurant are part of the same family that owns Commander's Palace and Mr. B's in New Orleans. And the landmark building in which Brennan's is located was modeled after the Iose Faurie house in New Orleans's French Quarter—now home of Brennan's on Royal Street (which is currently under separate ownership). Not surprisingly, the food here is best described as Texas Creole, which can mean an andouille jambalaya or a crawfish enchilada. A typical weekend brunch might begin with a Gulf Coast seafood gumbo, followed by *migas* (scrambled eggs with corn tortillas, tomatoes, jalapeños, onions, and Monterey jack cheese), and topped off with bananas Foster for dessert. In addition to a number of exquisite interior dining rooms, there's a lovely courtyard for outdoor meals. On Saturdays a Dixieland jazz band performs during brunch. Open Saturdays and Sundays from 10:30 A.M. to 2 P.M. (3300 Smith St., 713/522-9711).

KANSAS CITY

The Prospect of Westport

Sunday afternoons at the Prospect are such a Kansas City tradition that even for first-timers it's like spending a few hours with close friends. As soon as customers are seated, they're greeted with juice, coffee, or tea, and are invited to help themselves from the vast buffet in the center of the restaurant. The choices range from such old favorites as scrambled eggs, fried potatoes, and bacon to more offbeat fare like pasta pizza and rumaki pâté. The tables are set on two open levels around the buffet, which is in an atrium that soars up to a skylight. Wood and brick are complemented by hanging plants and ferns and colorful banners painted by students

from the Kansas City Art Institute. When the weather is nice, there's alfresco dining in comfortable shady enclave. Open Sunday only, 10 A.M. to 3 P.M. (1 Westport Sq. 816-753-2227).

LOS ANGELES

Michael's

"Modern American contemporary French cuisine with the feeling of eating at home," the way Michael McCarty describes the food at his renowned restaurant in Santa Monica. Since it opened ten years ago, Michael's has been touted by the likes of *Vogue*, *Esquire*, and *Connoisseur* (and all the major food magazines) and garnered numerous awards. Eating here is a very L.A. experience. At table either indoors or out, set with Christofle silver and Villeroy & Boch china, diners are su



How to get a cab in New York from an office in Los Angeles.



Actual Size

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FREQUENT TRAVELER

rounded by the rich and famous and artwork by David Hockney, Frank Stella, and Marcel Duchamp, among others. Somehow, ordering just fried eggs and sausage doesn't seem quite right in this atmosphere, even though it's entirely possible. More fitting dishes might be pizza with shiitake, tree, and chanterelle mushrooms or a molasses barbecue pork sandwich with grilled Maui onions. Open Saturdays and Sundays from 10:30 A.M. to 2 P.M. (1147 Third St., 213-451-0843)

MINNEAPOLIS/ST. PAUL

The New French Café

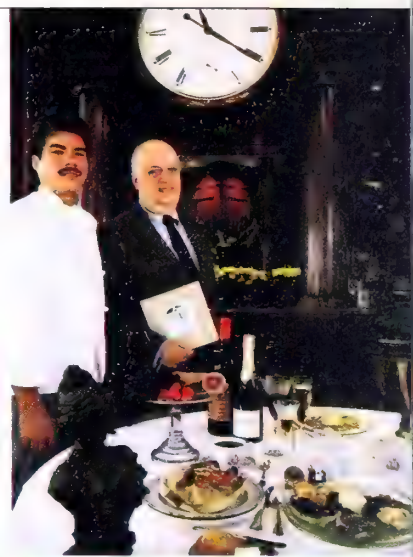
Despite its name, this popular Minneapolis spot has existed since 1977 in a part of the city known as the Warehouse District. Like New York's SoHo, artists moved into the area en masse back in the early 1960s after the buildings there were abandoned by wholesale clothing outlets and food shops. Many of the artists have since moved on because of rising rents, but the downtown district still retains much of its charm and artsy flavor. The New French Café fits right into the neighborhood. The dining area is a cavernous space, with exposed brick walls painted white, butcher-block tables, and bentwood-and-cane chairs. A massive espresso machine dominates the room, dispensing endless

cups of cappuccino. A few of the best brunch selections are salt cod patties with sauce remoulade and a tuna, garlic, and onion omelet with sour cream and capers. Open Saturdays and Sundays from 8 A.M. to 2 P.M. (128 North Fourth St., 612-338-3790)

NEW YORK

The River Café

The setting alone is reason enough to visit this spectacular restaurant. Situated on a barge on the Brooklyn shore of the East River, the spellbinding view encompasses the mighty Brooklyn Bridge, the busy water traffic of the river, and the imposing glass towers of lower Manhattan. Not surprisingly, the restaurant has served as the location for countless movie scenes. The dining room has a piano bar on one side and rows of well-spaced tables, all with sensational views. There's more. Over the years, the River Café has developed a reputation for being one of the premier all-American restaurants in the country. Featured on the two-course brunch menu are lobster baked in horseradish oil with oyster risotto, poached eggs on smoked-salmon waffles, and duck *confit* with roasted garlic and white beans. Open Saturdays from 12 P.M. to 2 P.M. and Sundays from 11:30 A.M. to 2 P.M. (1 Water St., 718-522-5200)



ST. LOUIS

Richard Perry Restaurant

Although this eatery is in a hotel (the Majestic), it's one of the best restaurants not only in St. Louis but throughout the Midwest—so it's an outstanding exception to our rule. Noted restaurateur Richard Perry just moved his namesake eatery to the hotel last year from a site on the south side of the city. Perry is known as a pioneer in American cookery; he was one of the first chefs to use fresh regional products in original ways. Many of the items on the menu are based on authentic, turn-of-the-century midwestern recipes. Some of the finest brunch offerings include a sautéed trout with almonds topped with poached eggs and sweet-potato fettuccini with shiitake mushrooms and smoked chicken. The restaurant itself has the look of an Old English club: cherrywood-paneled walls, mirrors, hurricane-style windows, and brass trim. Open for brunch on Sundays only, 10 A.M. to 2 P.M. (1019 Pine St., 314-771-4100)

SAN FRANCISCO

Tung Fong

Where to go for brunch in the Bay Area should never involve any decisionmaking. The answer is simple: a visit to a teahouse. Chinatown for dim sum. Minuscule Tung Fong (it has room for only about 20 Formica-topped tables) is one of the most remarkable of the city's dim sum houses. Upon seating, waitresses ask customers which of the seven house teas they'd prefer—included are jasmine and chrysanthemum. Next come the carts laden with Cantonese delicacies, baked, steamed, or deep-fried: a paper-wrapped chicken with barbecue sauce, dumplings with black-mushroom centers, succulent spareribs. At the end of the meal, the waitress counts the plates to determine the bill. But the pickled mustard greens and the hot black bean sauce are legendary, and they are available by the bottle. Open Saturdays and Sundays from 9 A.M. to 3 P.M. (808 Pacific Ave., 415-362-7115)



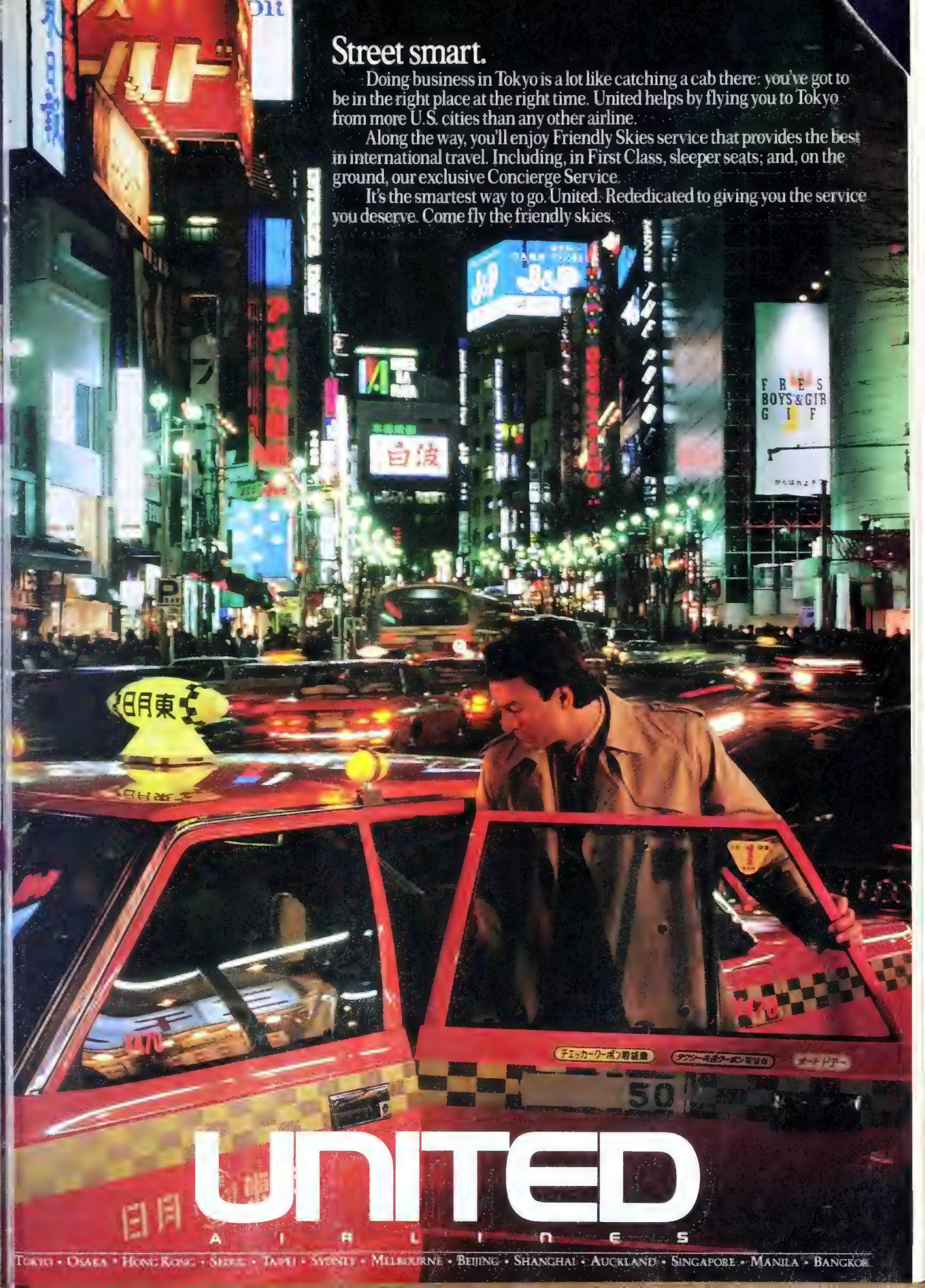
The incomparable view of lower Manhattan from the River Café (left); restaurateur Richard Perry and a member of his staff (above, right) present some of the St. Louis eatery's finest dishes.

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FREQUENT
TRAVELER

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THE PRICE IS RIGHT NOW
FOR LARGE, LUXURIOUS CARS

Most business travelers who spend a lot of time on the road are resigned to leaving luxury at home, especially when it comes to rental cars. But those long hours spent staring bleary-eyed at the interstate are exactly when the smooth ride and plushness of a classy car are most appreciated.

These days, price is no longer a reason not to take the luxury route—opting for a Cadillac or Lincoln Town Car instead of a no-frills econobox. Many car rental companies have not only added more top-of-the-line sedans to their fleets but also are now offering special discounts on these prestige cars. And because the rates are often comparable to those of midsize compacts, why not ride in style?

NEW YORK, NEW YORK

Thrifty has been on the luxury bandwagon for the past few years, with extremely reasonable prices for its snazziest cars. Currently a Chrysler New Yorker, the largest car in the company's fleet, costs \$34.95 a day, including unlimited mileage. This rate is a steal compared to that of other Thrifty cars, for example, the Dodge Dynasty (a full-size, four-door vehicle—a rung down from luxury) is more expensive at \$37.95 a day, and the average compact rate—for such cars as the Dodge Omni and the Plymouth Horizon—is only a few dollars less at \$32.71 a day. To qualify for the special price, reservations must be made more than 72 hours in advance. Call 800-367-2277.

In its dream-machine class, **Budget Rent a Car** features Lincoln Town Cars and Lincoln Continentals, both of which are available at nearly every location nationwide. The Cadillac Brougham and Cadillac Seville are also available in some areas. As a new bonus, the company has been offering unlimited mileage on all its luxury cars since February 1. With a three-day advance reservation, the cost per day is \$44.79, 24 hours ahead of time it's \$49.79, and the walk-up rate is \$54.79. Call 800-527-0700.

Members of **National Car Rental's** Emerald Club (a frequent-renter designation) are in the convenient habit of skipping all the paperwork by taking advantage of the Emerald Aisle, a lot full of ready-to-go cars. Customers simply take a bus out to the parking lot, hop in a car, and present their

membership card and driver's license to the gate attendant—a process that takes no more than a few minutes.

As an added perk, since St. Patrick's Day all the automobiles in the Emerald Aisle are now Cadillacs. Ranging from sporty to fancy, models include De Ville coupes and sedans, Fleetwood coupes and sedans, Brougham sedans, Sevilles, and Eldorado coupes, all of which are going for the same price as that of a midsize car (like a Buick Skyhawk or a Pontiac Sunbird). Rates vary depending on the location. Daily prices run from \$32.98 to \$69.98, weekly, from \$129.98 to \$279.98. There are 30 Emerald Aisles, most of them in major cities, and Emerald Club members don't have to reserve cars more than a few hours beforehand. Memberships cost \$50 a year.

Other luxury cars in National's fleet (that are available to nonmembers) include the Buick Park Avenue, Buick Riviera, and Oldsmobile Toronado. Rates range from \$41.95 to \$72.95 a day, depending on the location, and often include special mileage allowances. Call 800-CAR-RENT.

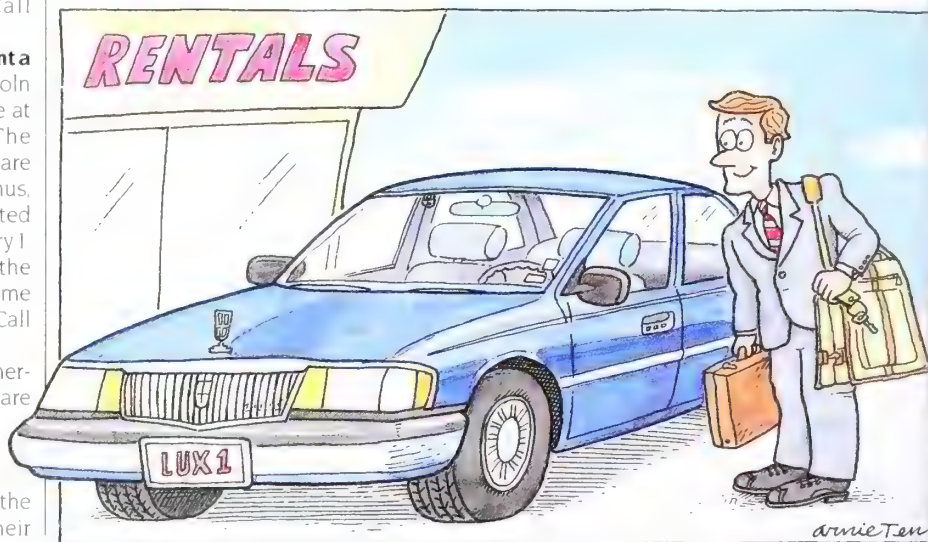
REMEMBER THE ALAMO

Alamo has recently reintroduced the Cadillac Brougham into Florida and is offering this car at the special daily rate of \$35.99, with unlimited mileage. On a national level, the company features the Buick Park Avenue

as its top-of-the-line vehicle. It also goes for \$35.99 per day—unlimited mileage included—in Florida and California, the two largest markets (prices vary elsewhere). This rate is only a few dollars more than that for Alamo's intermediate-size cars—such as the Chevrolet Corsica and the Pontiac Grand Am—which cost \$31.99 per day in Florida. Reservations must be made 24 hours in advance. Call 800-327-9633.

Hertz and **Avis** have also joined the luxury car race and often have special discounts, so it pays to check their prices. Avis has recently upgraded its selection of cars with more full-size, four-door sedans. The Cadillac Brougham and Cadillac Sedan de Ville are currently the company's top vehicles, with a daily rate of \$49 (these cars aren't available in Illinois or New York). In its premier class—a notch below luxury—Avis offers a line of four-door sedans outfitted with such luxe features as AM/FM stereos, tilt steering, cruise control, and automatic locks. Included are the Buick Park Avenue, Buick Le Sabre, and Pontiac Bonneville. Call 800-331-1212.

Hertz's largest sedans are Lincoln Town Cars, Lincoln Continentals, and such Cadillacs as the Brougham, Sedan de Ville, and Seville. Prices go from \$49.90 to \$79.99 a day, depending on the location. Watch for another Hertz discount on luxury autos this spring. Call 800-654-3131.





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No lines. Nothing to slow you down.*



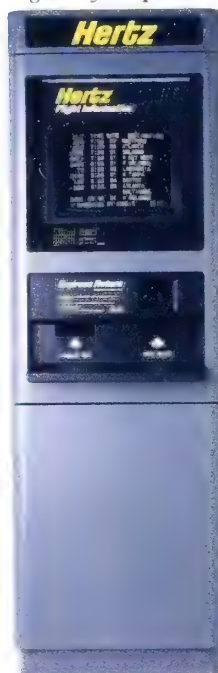
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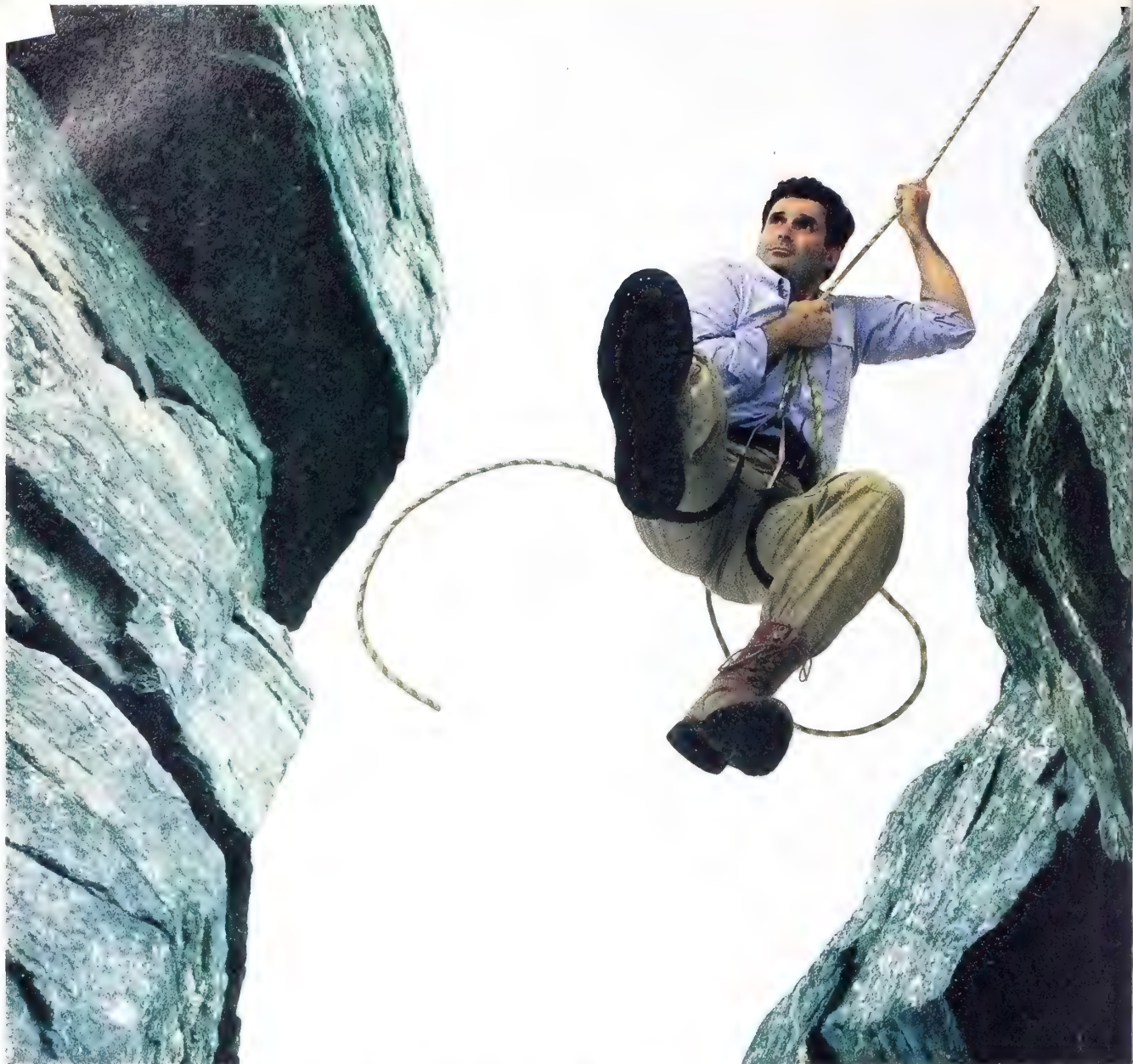
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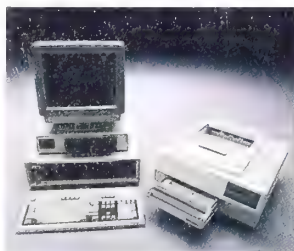
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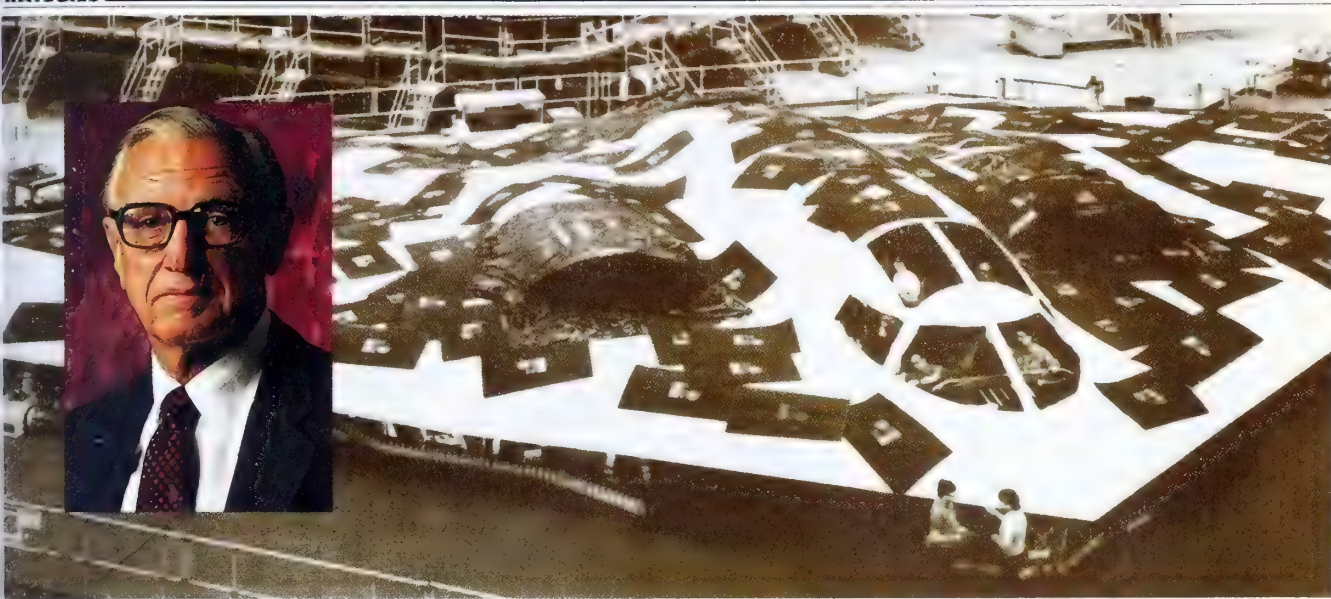
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ROUND ZERO: CHAIRMAN JONES FACES A BRIBERY PROBE, AND NORTHROP'S PRODUCTION OF THE B-2 HAS BEEN DELAYED NEARLY TWO YEARS

NORTHROP IS FLYING IN A SKY FULL OF FLAK

167-count criminal indictment is the latest blow to the beleaguered B-2 bomber's maker

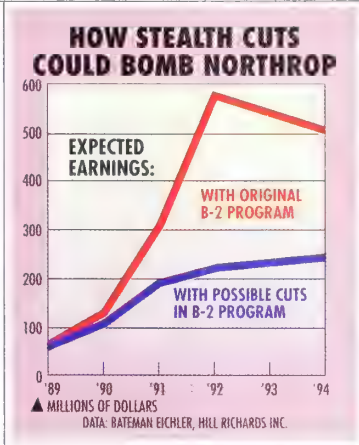
Seven years after snaring one of the biggest military contracts in history, Northrop Corp. threw itself a party last November. While crowds cheered and a marching band played, the contractor unveiled its super-secret, radar-evading Stealth bomber. Five months later, there is no trace of euphoria left. While Northrop was waiting to see whether new Defense Secretary Richard B. Cheney would propose major cuts in its Stealth, or B-2, bomber program, the company was hit on April 1 with a 167-count criminal indictment. The charges: Northrop supplied defective parts and falsified test results on key components of the Air Force's air-launched cruise missile and the Navy's V-8B Harrier jet. If convicted, Northrop faces fines of more than \$30 million. More immediately, Northrop could be suspended from doing business with the Defense Dept., even if only for a few months. The company denies all the charges.

The indictment is hardly Northrop's only legal woe. Another federal grand jury is looking into whether the company and Chairman Thomas V. Jones bribed a South Korean lobbyist in 1983 to get the Asian nation to buy the con-

tractor's F-20 Tiger shark fighter jet. And the Justice Dept. recently joined two of several civil lawsuits filed under the False Claims Act by former Northrop employees. One of the whistleblower suits, which Justice joined in March, also accuses Northrop of falsifying test data on the Air Force cruise missile parts and seeks \$63 million in damages and fines. What's more, Northrop may yet be named in the Pentagon's sweeping investigation into bribery, bid-rigging, and fraud called Operation Ill-Wind.

The prospect of multimillion dollar settlements or fines is daunting for Northrop—particularly since it is already straining under heavy debt and the threat of a drastic slowdown of its B-2 program.

Under pressure to cut \$60 billion over five years from the defense budget, Defense Secretary Cheney is expected to ask President George Bush to stretch



out delivery of the 132-plane order—and payments to Northrop—over more years than the six originally scheduled.

Northrop's worst nightmare: Once the B-2 production schedule is lengthened, congressional Democrats would have more time to slash the program further—or eliminate it altogether. That would be disastrous for Northrop, which gets 50%

of its \$5.8 billion in annual revenues from the B-2 program.

To make matters worse, the company's overall revenue growth has been slow for the past three years, largely because Pentagon funding for B-2 research has been winding down and production delayed. Northrop had to take a \$150 million write-down in 1988 because of cost overruns on other secret projects. The result: Northrop made a \$104 million profit last year but would have lost \$31 million if not for a onetime tax adjustment. No wonder, then, that the



Hottest rental. 2007 A.D.



The VCR you'll play it on. 2007 A.D.

What movie will be the blockbuster of 2007 A.D.? Hard to say. But one thing's for certain. Samsung VCRs will definitely be getting rave reviews.

SAMSUNG
The future of electronics.

stock price has been languishing close to its postcrash low of 25.

Northrop had been counting on the B-2 to bolster its numbers. It says the first plane will fly by early summer, nearly two years behind schedule. Originally, the Air Force had hoped to be receiving 36 planes a year by 1992. Under that scenario, Northrop's earnings would have risen more than fivefold, to \$58 million, says Lawrence M. Harris, an analyst with Bateman, Eichler, Hill Richards Inc. Even by modestly stretching out the delivery schedule to 10 years, say, instead of 6, Northrop's earnings would double, to \$229 million by 1999, says Harris (chart). Stretching out deliveries could increase the risk that the government would cut back the number of planes it buys.

Northrop executives are unfazed by the potential cutbacks. "We are delighted," says President Kent Kresa, "with progress on the B-2." Before it got the B-2 in 1981, Northrop largely produced less pricey fighter planes that it sold to foreign buyers. Built of radar-evading composite materials, one key mission of the B-2 is to seek out and destroy the latest generation of Soviet mobile missiles. But critics say the price tag—a \$68.1 billion for 132 planes—is too hefty.

Northrop's most pressing concern, obviously, is defending itself against U.S. Attorney Robert C. Bonner's indictment. He charges that Northrop knowingly supplied cruise missile flight-data transmitters that failed to perform at the extremely low temperatures required by the Air Force. Bonner also charges that supervisors often falsified test results on the transmitters, some 1,750 of which have already been installed on missiles. Says a company spokesman: "The criminal charges are unwarranted, and the company strongly disputes them."

SUSPENSION. The Air Force is mulling whether to recommend suspending Northrop from defense work. That would halt any payments on current contracts or new awards until the government is satisfied that Northrop has cleaned up its act. In earlier fraud cases, suspension has amounted to just a few months.

If the company is indicted in the Korean case, Chairman Jones, who has run the company for 28 years, may be vulnerable. If convicted, he would be in violation of a consent decree he signed back in 1975. By signing the document, he agreed not to bribe foreign officials without admitting or denying guilt to charges that he and the company made \$30 million in illegal payoffs to foreign officials. Jones refused to comment on any of his legal problems. For now, he and Northrop have little choice but to sweat it out on all fronts.

By Eric Schine in Los Angeles, with Paul Dwyer and Dave Griffiths in Washington



Four Seasons Chairman Isadore Sharp dismisses fears of a Maui glut. And he has taken steps to minimize the risks. The company has been able to accelerate its expansion by using other people's money. Four Seasons has no equity stake in the Maui resort, nor does it in hotels opening in 1991 in Tokyo and Mexico City. And it will own only a 15% interest in a resort on the Caribbean island of Nevis that opens in 1990. But such outside equity sources could dry up if projects turn out to be duds.

HIDDEN VALUE. Four Seasons' worries are limited primarily to filling the house. It gets a management fee, which typically starts at 3½% to 4% of total revenue, providing steady income. The financial risk is borne by the resorts' owners. For instance, the owners of the Maui resort, TSA International Ltd. and Shimizu Corp. of Japan, must cover the expected debt-service shortfall in the first three years of operation.

Sharp's formula for attracting discerning vacationers: Budget \$300,000 or more per room—double the resort industry average—for top-notch construction and furnishings. Provide access to tennis, golf, and beaches, but keep the properties small and casual enough that it's more like a stay at a wealthy friend's vacation home.

Investors like the story. Four Seasons' stock price is up 38% in the past 12 months, thanks to a 16% rebound in 1988 earnings, to \$11 million on revenues of \$503.8 million. Management fees are expected to spurt because six of Four Seasons' contracts are nearing the point at which they will generate incentive fees of 15% to 20% of the hotels' after-tax income. That could mean 15% annual earnings growth over the next five years.

Indeed, with little debt, and plenty of hidden asset value—Four Seasons owns all or part of 11 of its prime properties—investors are standing in line for the stock. "We know the public float is too small," says H. Roger Garland, executive vice-president for finance. But don't look for a change. The company isn't hurting for cash, and the 57-year-old Sharp, who founded the company 28 years ago and holds 83% voting control, isn't anxious to dilute his stake.

Sharp isn't letting up. He will open as many as 15 new hotels and resorts in the next five years. He rejects the notion that it will stretch the company thin. "It's a myth that quality and growth are incompatible," he says. He has already proved that. What's left for Sharp to prove, however, is that vacationers will spend their own money on what Four Seasons has to offer.

By Chuck Hawkins in Chicago

FOUR SEASONS LEADS FOR THE BEACH

he hotel chain dives into the waters of plush resorts

Four Seasons Hotels has an intimate grasp of its market. Whether at the Inn on the Park in London or the newly opened Four Seasons Hotel in Chicago, the hotelier gives its clientele—traveling doctors, lawyers, and senior business executives—the kind of pampering they expect. Not only does the staff scramble to fulfill the tiniest request but the rooms are among the shiest in the industry. Guests aren't likely to quibble with rates that are among the highest in each of its 22 markets, either. After all, the chain usually ends up on an expense account. Now, Toronto-based Four Seasons Hotels Inc. is about to venture out of that protective niche. The company is betting it can draw vacationers to the six to eight luxurious resorts it's planning to build.

TOUGH TIMES. The problem is that several competitors have the same idea. When its 374-room hotel opens later this year on the Hawaiian island of Maui, room rates will be aggressively priced at an average \$280 a night. Most of the oversized rooms will have breath-

taking ocean views. But so will many of the 800 rooms at the Grand Hyatt resort hotel going up next door. And down the road, a 550-room Ritz Carlton will soon be built. "It looks like rough times for all of them," says Saul F. Leonard, a lodging consultant for Laventhol & Horwath.

LUXURY RESORT DEVELOPERS

HYATT Developing properties in Colorado, Aruba, Bali; 800-room Wailea Grand Hyatt on Maui will have 15,000-sq.-ft. pool, second one 2,000 ft. long

RITZ CARLTON Resorts planned for Colorado, California, Florida, Puerto Rico; hauling millions of cubic yards of white sand to Mauna Lani resort on Hawaii

FOUR SEASONS Projects in Hawaii, Caribbean, Far East; will ferry guests to getaway on island of Nevis

INTER-CONTINENTAL Development under way in Denver and Mexico, plus \$24 million renovation of Maui property

WESTIN Two on the way, including a venture near Walt Disney World

DATA: COMPANY REPORTS



WHO DO YA LIKE? AT THE SPORTS BOOK IN THE HILTON LAS VEGAS, BETTORS CAN WAGER ON EVERYTHING FROM NCAA BAS

AMERICA'S GAMBLING FEVER

EVERYBODY WANTS A PIECE OF THE ACTION—BUT IS IT GOOD FOR US?

Every evening thousands of bingo players around the country lay out their cards, focus their eyes on video monitors, and start playing Mega-Bingo. Launched last February, it's the world's biggest and richest bingo game, with a \$500,000 jackpot. Numbers drawn in a Tulsa bingo hall are telecast live via satellite to 15 other halls in eight states.

- In South Dakota, the legislature recently authorized the installation of new video gambling devices—electronic near-equivalents of slot machines—in bars and taverns. Within a year, 2,500 of the machines should be in operation.
- In Maryland, Pimlico Race Course has just opened its huge "Sports Palace."

Horseplayers can put bets on the Pimlico card and on races "simulcast" live from a dozen other tracks on huge TV screens. They can also watch an array of other sports events while keeping an eye on a mural-size display of hundreds of scores and betting lines. Betting on sports such as football and baseball is illegal anywhere but in Nevada and Montana. But Pimlico's owners are getting set for its legalization nationally, which some observers believe will happen within a few years. The Pimlico Sports Palace could then become the country's largest sports-betting casino.

- In Iowa, the state lottery recently began producing live TV game shows with

teams of lottery players as contestant. Ratings have been higher than those for *Wheel of Fortune*, in part because the shows also announce prizes for players at home. Lottery officials are considering arranging for home viewers to play along by calling in answers with touch-tone telephones.

At a pace that seems almost epidemic, gambling fever is sweeping the U.S.—and raising disturbing questions about its possibly deleterious impact on society. Today gambling outlets are almost as ubiquitous and well-patronized as convenience stores. Gambling is part of the weekly, and even daily, routine of tens of millions of Americans—and of mar



PROFESSIONAL BOXING MATCHES



HORSEPLAYER HEAVEN: HANDICAPPERS AT LAS VEGAS' STARDUST HOTEL



ARMLESS BANDITS: VIDEO POKER GAMES ARE THE CURRENT CASINO CRAZE

ions more in Europe, the Far East, in America, Australia, and Canada. University of Nevada gambling expert William N. Thompson puts it: "The old seems now to be engulfed in a table explosion of expanding gambling activity." Last year, says industry consultant Eugene Martin Christiansen, Americans legally and illegally wagered more than \$240 billion, a figure that is rising at about 10% annually.

H-TECH TINHORNS. New gambling technologies are driving much of that growth. They have propelled the boom in lottery business and revitalized the sluggish casino and horse-racing industries by making betting easier, quicker, more exciting, and more seductive. New versions of slot machines and card games, say casino executives, are captivating younger players raised in the video age. Credit and debit cards are beginning to replace cash. Lottery players can place bets through automated ticket dispensers and soon will be able to use cash machines and terminals in supermarket check-out lanes.

The most lucrative future betting paradigm, many gambling executives believe, will be the living room. They have a vision of millions of couch potatoes watching sports contests and other

events while they bet early and often by flicking special buttons on their remote-control wands. Already, Pennsylvania horseplayers at home can watch live racing from three local racetracks on cable TV and phone in their bets.

Gambling fever also stems from a remarkable change in public attitudes toward the pastime over the past decade or two. For much of this century, gambling was generally regarded as a pernicious vice, only slightly less unsavory than prostitution. It was thought to breed crime and corruption. Most organized gambling was popularly associated with the Mafia.

Gambling's stigma has not been erased—as the controversy over allegations of illegal gambling by Cincinnati Reds Manager Pete Rose attests. But that incident is an exception. "We may have crossed a historic watershed," says Eugene Christiansen. "Gambling has gone through cycles of being prohibited and legalized. But now, for the first time, it is being legitimized. It's coming into the American mainstream." Adds Michael Rumbolz, former head of the Nevada Gaming Control Board who now runs Donald Trump's Nevada operations: "You have a whole new generation of people who feel they can

gamble without thinking that it reflects poorly on their character."

A big reason is the clean-hands image of the folks now running most of the games. Mob-affiliated bookies and numbers runners are being supplanted by state governments, charitable and religious groups, and blue-chip entertainment-leisure conglomerates that say they're in the "gaming" business. Like mob bosses before them, the new proprietors covet gambling's inexorable, cornucopian cash flow. But unlike the mob, they spend millions on sophisticated market research and advertising campaigns. Recent federal legislation will remove next year most constraints on lottery and charitable game advertising.

NUMBERS GAME. Alchemizing vice into virtue, state lotteries glamorize the same activities that could get you five years in the slammer—if you had the misfortune to get caught running a numbers racket. Some countries, mainly in Europe, have run lotteries for centuries. But never before have governments worked so



hard to entice citizens to become gamblers. Facing budget deficits and intense anti-tax sentiment, states see lotteries as a magically painless revenue source—they will net more than \$7 billion this year. Lotteries are no panacea: They account for less than 5% of the budget in most states that have them. Still, they help pay for many important state services, such as education.

The new proprietors are helping to change the fundamental character of gambling. It was once a circumscribed world of seasoned players who tended to prefer games requiring skill, such as poker and horse racing. To attract millions of new players, points out Pennsylvania State University sociologist Vicki Abt, the new proprietors are "de-skilling" gambling: Millions of people can't be expected to learn how to handicap horses. The most popular attractions now, such as lotteries, slot machines, and bingo, are games of pure chance. And while skill-intensive games have relatively short odds, and thus low payouts, the chancier games increasingly feature long odds and giant jackpots, which have proved enormously effective in recruiting new lottery players. While seasoned gamblers are caught up by the action of the play, newcomers are mainly interested in the size of the payoff.

HEALTHY? Gambling fever also is giving fresh urgency to the ongoing debate over gambling's impact on society. "Playing the lottery is a form of recreation that's no more harmful for most people than going to the movies or bowling," says Iowa Lottery Commissioner Edward Stanek. Industry leaders would say that applies to all forms of gambling. It is also, they say, a healthy escape from the frustrations of modern society: For a mere dollar, the bettor can fantasize about that life-transforming pot of gold at the end of the rainbow.

But a small, vocal band of critics is challenging this view. They concede that gambling is a remarkably pervasive and enduring phenomenon that satisfies deep psychological needs. And they agree that in moderation gambling, like

alcohol consumption, is probably benign. Few believe it should be prohibited.

But the impetus to gamble, as the growth of state lotteries graphically shows, seems unusually responsive to stimulation by advertising, availability, and the allure of a game's design. That, critics feel, raises some difficult issues: Should governments be in the business of actively promoting gambling and using the proceeds as a substitute for tax revenues? "You're marrying the government's insatiable revenue needs with

of them teenagers who seem most venerable to the industry's blandishments. Is gambling fever Main Street's way reflecting Wall Street's obsession with short-term speculation instead of long-term investment? Is it fostering a natural bias away from skill and hard work toward luck and fate as the best road to success?

BOOMTOWN. Luck and fate are most curiously enshrined, of course, in Las Vegas, and there is no more visible symbol of gambling fever. In eclipse a few years ago, Las Vegas today looks like gold-rush town, which in a way it is. Tourism is booming. Gargantuan new hotel/casinos are rising from the desert—and along the beach in Vegas' East Coast spring, Atlantic City.

Vegas has become adept at marketing itself as a resort and convention center. In much of its new prosperity comes from slot machines. "Table games," such as blackjack, still account for the bulk of the wagering. But slots now produce as much as 80% of some casinos' gambling profits. New technology is the reason. Electronic slots, far more versatile than mechanical ones, have been linked into "Megabucks" networks comprising numerous casinos. Thanks to larger numbers of players, they can offer multimillion-dollar payoffs. They have also been configured in video versions of table games, which new players find much less

intimidating than facing a live dealer. The current craze is video poker, the Nintendo of the video-gambling world. Video poker doesn't exactly offer the rich nuances of William Tell outbluffing an opponent. But it is able to hook players by adding just a touch of skill to what is basically a game of chance.

Over the past decade or so, some two dozen campaigns to legalize casinos beyond Las Vegas and Atlantic City have been launched in such places as Michigan and Detroit. But all were either abandoned or rejected by voters or state legislators, who were more nervous about the taint of organized crime still surrounding Vegas-style gambling than

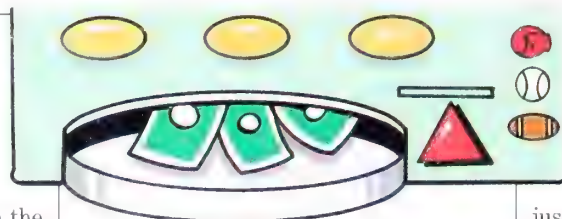


WHERE THE ACTION IS

	1988 total wagering Billions	Percent increase 1983-88	1988 revenues (net of payoffs to bettors) Billions	Percent increase 1983-88
LOTTERIES	\$17.1	229.7 %	\$8.4	176.7%
CASINOS**	161.9	52.7	7.1	52.9
SLOT MACHINES	37.3	98.6	4.0	70.2
TABLE GAMES	124.6	42.9	3.1	34.9
PARI-MUTUELS**	17.6	20.5	3.5	24.6
HORSES	13.7	17.3	2.8	22.3
GREYHOUNDS	3.2	40.3	0.6	38.0
JAI-ALAI	0.7	7.1	0.1	16.2
LEGAL BOOKMAKING**	1.8	117.0	0.1	126.3
BINGO**	4.1	34.7	1.0	24.4
OTHER CHARITABLE GAMES**	2.3	64.5	0.8	73.8
CARD ROOMS	3.1	197.0	0.3	380.8
INDIAN RESERVATIONS	0.4	NA	0.1	NA
ILLEGAL GAMBLING**	32.3	12.2	5.6	12.3
SPORTS	20.7	14.3	1.8	15.0
HORSES	6.1	4.6	1.0	4.6
NUMBERS	5.5	13.5	2.8	13.7
TOTAL	\$240.6	49.6 %	\$26.9	59.6%

*Gross wagering figures tend to overstate casino betting, where winnings usually are quickly bet on the next game
 Estimated *Preliminary NA—not applicable

DATA: CHRISTIANSEN/CUMMINGS ASSOCIATES INC., GAMING & WAGERING BUSINESS



people's propensity to gamble," says Christiansen. "It's a vicious mechanism." Are lotteries preying on the poor, who most need an escape from society's frustrations? "It's just about the most regressive tax around," claims Philip J. Cook, a Duke University economist. Other questions about gambling are equally troublesome: Will gambling fever create millions of compulsive gamblers, many

used by its potential economic benefits. Ironically, gambling interests fearing competition, especially the casino industry, helped orchestrate the opposition to any of these initiatives.

Yet the cards may be turning. South Dakota recently authorized casinos in the Old West town of Deadwood. One house of the Ohio legislature voted to permit casinos in Lorain, an ailing Lake Erie steel town.

VERBOATS REDUX. Meanwhile, less conspicuous casino-style endeavors are proliferating. Cruise ships outfitted with gaming tables and slot machines regularly operate from ports in Florida and Texas. Several states, including Iowa, Illinois, and Mississippi, are considering bringing back a sanitized version of the verboat gambler by letting floating canoes ply the Mississippi River.

Nine states permit card clubs. Originally legalized to exempt back-room poker games from antigambling statutes, the clubs are becoming a big business. The Bicycle Club near Los Angeles, one of 350 clubs in California, has 155 tables, attracts 2,000 players daily, and grosses \$3 million a year from seat-rental fees charged to players who then bet against each other. A loophole in a new Arizona law allowing "social gambling" has spawned dozens of minicasinos offering blackjack, craps, and roulette in Phoenix and Tucson. In Montana, 8,400 video-gambling machines operate in bars and retail stores, and betting—\$255 million in 1988—has doubled each year since legalization in 1985. Like South Dakota, Montana legalized these machines most because so many were already operating illegally. "Gray-market" video dealers are spreading nationally.

Perhaps the most pervasive form of gambling is charitable games, principally bingo, run by churches, fraternal groups, and myriad other organizations. Charity bingo, legal in 46 states, is no longer a little-old-lady, church-basement affair. Professional bingo promoters help charities run weekly or even nightly games in large halls that gross millions of dollars a year. Electronic bingo dealers, which have lured hordes of new players in Canada, are heading south. Growing numbers of states allow charities to hold "Las Vegas Nights," featuring casino-style table games. Maryland recently voted to allow social and religious groups in several Eastern Shore counties to run slot-machine complexes. Gambling fever is also spreading to horse racing. Only a few years ago many experts felt it was a dying sport. Now attendance is soaring, new tracks are being opened, and the roster of states allowing pari-mutuel betting, now 12, is growing. Greyhound racing, now banned in more than 50 tracks in 15 states, is expanding even faster. Technology

BINGO! ARE INDIAN TRIBES HITTING THE JACKPOT?

Just five years ago, with federal funds cut back and few job opportunities, the outlook for impoverished members of the Muscogee (Creek) Nation in Oklahoma was bleak. Then the Creek Nation introduced bingo. Today five bingo halls on Creek land annually attract 50,000 visitors, mostly whites, who wager more than \$22 million. That gives the Creeks a net profit of better than \$3 million, which is spent on health care, education, and social services. More important, bingo employs some 225 Creeks, with a monthly payroll of \$150,000. The game, says William E. Foster, Creek gaming commissioner, "has been a very successful economic development project."

As much as \$350 million is wagered each year in legal gaming (mostly bingo) on some 120 of the 310 reservations in the lower 48 states. Outside management companies, which run most of the games for the Native Americans, get as much as 40% of the money bet, leaving the tribes with a 12% to 18% piece of the action. The rest goes out as prize money.

ELECTRONIC POKER. Because of their sovereign status, Indian tribes operate gambling operations with little state oversight. If a state permits some form of gaming, say, church bingo, a tribe can then offer it on Indian land without state restrictions. Federal legislation passed last year, however, requires tribes to negotiate with states if they want to operate more advanced gambling, such as casino games and horse and dog betting. Nearly all

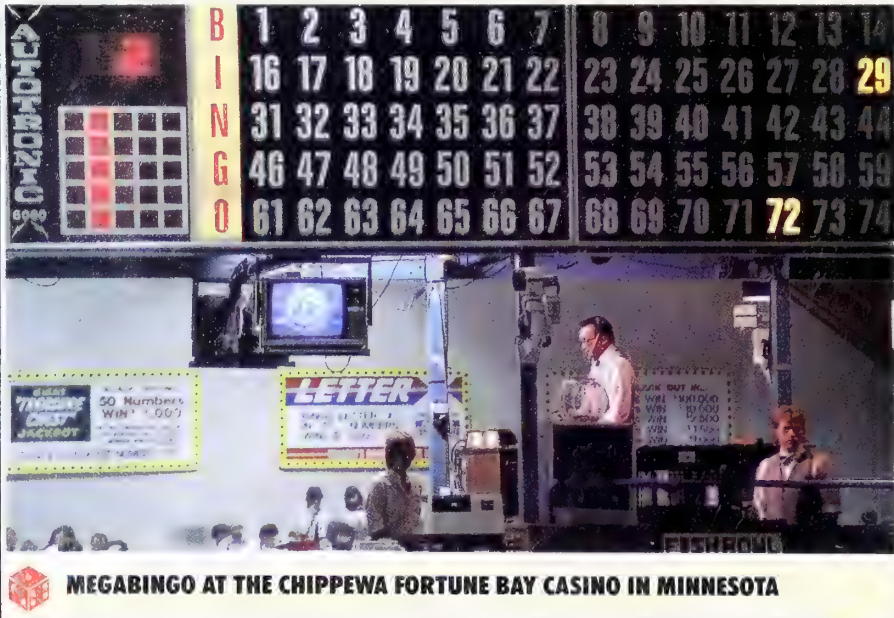
of Montana's tribes have submitted petitions.

Many tribes are already involved with activities that go beyond simple bingo games. Gamma International Ltd., a management company, operates MegaBingo, which links via satellite bingo halls owned by 15 Indian tribes. It offers a combined nightly pot of \$10,000 and a chance at a \$500,000 jackpot. Gamma expects players to wager \$30 million this year and double that in 1990. The Bois Fort Minnesota Chippewa tribe's plush Fortune Bay Casino north of Duluth has electronic poker and lotto machines. A law passed by Congress will permit Indians next year to advertise gambling nationwide.

Gambling is not all found money for America's Indian tribes. Large amounts of cash and lax record-keeping invite crime. In February an anonymous witness at a Senate hearing on Indian corruption testified that organized crime has infiltrated gaming operations on a dozen reservations. "You don't need organized crime. You can have disorganized crime—skimming, cheating—the temptation is there," says I. Nelson Rose, a professor at Whittier College School of Law and a gambling law authority.

Most tribes, many of whom dwell on remote, inhospitable land that neither supports agriculture nor attracts industry, seem willing to take the risk. For them, legalized gambling is as close as they will ever come to hitting the jackpot.

By Sandra D. Atchison in Denver

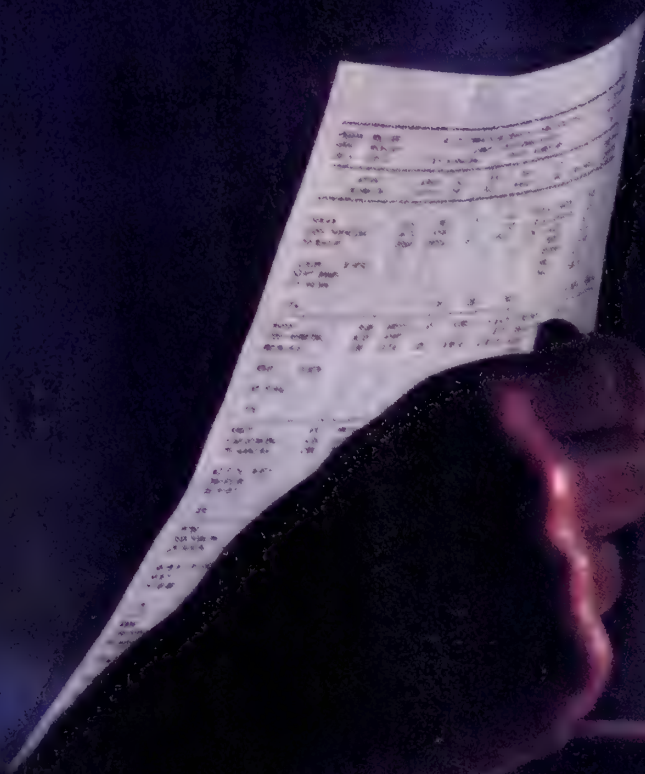


MEGABINGO AT THE CHIPPEWA FORTUNE BAY CASINO IN MINNESOTA



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Cover Story

has made track action faster and more exciting. In addition to daily cards, many tracks now offer patrons action on races at other tracks. The sport of kings also lures the commoners with such popular high-stakes wagers as exactas and trifectas, which, to novices, are basically luck bets.

Growing numbers of mostly track-run off-track-betting (OTB) parlors and "teletheaters," which televise races live, are attracting new players. Many OTBs permit telephone betting. Tracks get a slice of the off-track action. But to make sure players keep coming out to the ovals, they are constructing elaborate racing centers, such as Pimlico's Sports Palace, with casino ambiences.

For many years it appeared that lotteries, offered by 33 states, were destined for the same limbo predicted for the racing industry. Government-sanctioned lotteries during the 18th and 19th centuries eventually either collapsed or were banned because of scandals. The current lottery era, beginning with New Hampshire in 1963, was nearly aborted for lack of interest. But increasingly sophisticated automation permitted lotteries to raise the frequency of drawings from monthly to weekly and daily, to introduce instant tickets, to switch from passive to active games where players could pick their own numbers, and, most recently, to roll out giant-jackpot lotto games. Each enhancement, especially lotto, precipitated a sharp sales jump.

Yet the "play value" of most lottery games—buy your ticket, wait for the drawing—pales beside even your basic mechanical slot machine. Lottery players are soon bored. "You have to keep coming up with a new improved, improved Ivory Snow," says Massachusetts Lottery Director James E. Hosker.

'ELECTRONIC CASINOS.' Several states, notably Ohio and Oregon, have installed self-service, ticket-issuing terminals in retail outlets. The biggest leap forward may be the video lottery terminal (VLT), which walks and quacks very much like a video slot machine. VLTs have stirred intense controversy and opposition. "You're having governments effectively running electronic casinos under the guise of the lottery," says University of Nevada gambling expert William R. Eadington. A highly successful test of 400 VLTs in Nebraska in 1984 was abandoned after protests from local race-

track interests. However, Charles Mathewson, chairman of International Game Technology, which makes VLT machines, claims they will be "the growth industry of the nineties."

Lottery directors don't want to wait that long. Like racetrack owners, they are eyeing the \$20 billion, illegal, sports-betting market. The Super Bowl alone generates an estimated \$2.5 billion in illicit wagering. Since most lotteries are barred from operating games of skill,

ting, meanwhile, is more and more in the open. Many newspapers publish daily betting lines. Next summer the Gaming Network, a new Las Vegas-based satellite-TV facility, will start sending 12 hours of daily gambling information, including the latest betting lines, to cable systems. Legal sports betting, says New York acting Lottery Director Russell V. Gladioux, is "on the horizon."

In case it isn't, lottery directors and racetrack owners have another idea.

Iowa is only one of several states considering expanding current TV game shows of lottery players to include at-home, over-the-phone betting using credit or debit cards. While it would face formidable political and legal challenges, the ultimate hook for many lottery and track people, think, would be interactive home betting on live TV game shows and sports contests. Says Larry Charles, U.S. creative director for Hill & Knowlton Inc., who has discussed the idea with several lotteries: "This would allow the customer to play and win on impulse with immediate gratification."

PROGRESSIVE PLAY. All the above terrifies critics of gambling fever. They believe that the even more-intense volume of inducements with which the gambling industry is enticing people will inevitably lead to excesses. Some critics favor the British policy toward gambling: Allow it, but don't allow it to be "stimulated."

The critics are especially incensed by "turning Uncle Sam into the Godfather," as University of Notre Dame Professor Robert Blakey has put it. Capitalizing on their inherent legitimacy, state lotteries have recruited tens of millions of first-time gamblers. States such as California and Massachusetts have achieved participation rates



BIG HIT: BLACKJACK AT AN ARIZONA MINICASINO

they are exploring largely chance-based sports pools, where the player, for instance, would have to pick the correct winning margins for a large number of games. Sports pools are already being offered by lotteries in Europe and British Columbia, Canada.

But there are plenty of roadblocks. Professional sports leagues, especially the National Football League, maintain that legalized gambling would corrupt games. Yet, while an NFL spokesman dismisses the possibility, lottery directors feel an accommodation will be worked out. The NFL knows that bettors help fill stadiums and hike TV ratings. Sports bet-

ting in some games of more than 80% of the adult population. Evidence suggests that once people start playing the lottery they often progress to other forms of gambling, including illegal gambling. Law-enforcement officials say state sponsorship of legal gambling has spurred illegal betting by helping wipe out gambling's stigma.

Critics also castigate lotteries' sales pitches, which stress the fantasy of huge jackpots but say little about the often astronomical odds against winning and the low payout. Typically only 50% of a lottery's sales is returned as prizes to players. Racetracks and casinos offer



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pay out 80% or more. Says Penn State sociologist Vicki Abt: "The lottery is the worst game in town."

In a forthcoming book on lotteries, Duke Professors Charles T. Clotfelter and Philip J. Cook write: "It is troubling that the fantasy is sustained to such a large extent by ignorance and delusion." That a state should even be in the fantasy business is curious. "Here you have the same outfit that is trying to educate our children selling images and hyperbole rather than factual information—and telling the public: 'Play your hunch,

you could win a bunch,'" says Cook.

Critics are most disturbed by the lotteries' economic impact on poor and working-class players. Clotfelter and Cook cite evidence that poorer people spend a much bigger portion of their income on lotteries than high-income players do. Because huge lottery jackpots concentrate payouts, most lottery players lose most of their wagers.

Gambling's possibly noxious side effects extend far beyond lotteries. Critics are very worried about compulsive gamblers, who are unable to control their

betting and who seem most vulnerable to gambling hype. Research on the subject has been scanty. But Richard Richardson, head of the Maryland Council on Compulsive Gambling, claims the problem "has reached epidemic proportions. Compulsive gamblers, who become most addicted to fast-action casino and sports betting, make up only 3% to 4% of those who gamble. But an additional 10% to 15% bet more than they can afford. Robert L. Custer, an authority on compulsive gambling, says these two groups may account for close to half of all money wagered. No surprise, then, that the gambling industry has shown only token interest in the problem: Compulsive gamblers are often their best customers.

TEENAGE PLAYERS. Especially troubling is the surge of gambling by teenagers. According to a 1987 study of New Jersey high school students by Henry R. Lesieur of St. John's University, 86% had gambled in the past year, and 32% had gambled at least once a week. At Atlantic City casinos, where gamblers must be at least 21, turned away 200,000 minors in 1987 and escorted an additional 35,000 from their floors. But often no one is around to keep minors away from automated gambling machines, such as player-activated lottery terminals.

The specter of the living room as a family casino, says Custer, could be "disastrous. I just don't think Americans would be able to control it when it is so available. It would be too tempting, not just for the parents but the whole family. The kids would be saying: 'Bet my allowance on the Bengals.'"

And what, finally, about the work ethic in the face of high-powered fantasy marketing? A newspaper story on lottery jackpot winners said they could "forget scrimping and saving and all that Horatio Alger stuff. They found the instant route to wealth in America. How will we compete against the Japanese with that sort of philosophy?"

Other than a few disgruntled academics, law-enforcement officers, and religious moralists who aren't running bingo games, nobody seems especially concerned about gambling fever's downside. The state likes gambling. The church likes it. Business likes it. And the people, most of whom are now gambling, like it. We can't and shouldn't try to stop people who want to gamble from laying down a bet. But unlike the British, we're doing a lot more than just accommodating betting. We're letting legions of promoters inveigle people to be as much as possible. That policy could get us as a nation hooked on gambling in ways we never bet on.

By Chris Welles in New York, with bureau reports

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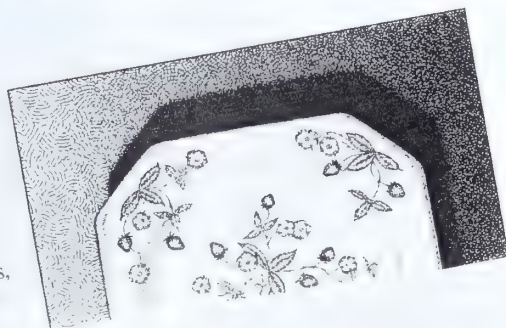
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STUFFING NEST EGGS WITH ESOPs

How companies are linking performance and pensions

Employee stock-ownership plans are hot. On Apr. 11, Northwest Airlines Inc. said it was thinking about an ESOP. The week before, Lockheed Corp. announced a \$500 million ESOP giving workers a 17% stake, while Tribune Co. expanded its employee ownership from 1% to 10% through a \$350 million ESOP. Recently, Polaroid Corp.'s employees acquired some 20% of the company.

Keeping real or rumored raiders at bay is nearly always a prime motive, but not the only one. "We believe greater stock ownership ought to serve as a catalyst for better job performance," says James M. Eastman, vice-president of employee relations at Federal-Mogul Corp. Turning employees into capital-owners can, the argument goes, lead to rising productivity—and a higher stock price.

It better. The ESOP movement is making the fates of companies and their employees more intertwined than ever. Newly enfranchised employees are a shareholder bloc that could be crucial in a takeover contest, and how well the company and its stock performs in the long run is becoming critical to the adequacy of rank-and-file pensions.

"The ESOP in blue-chip companies is emerging as a significant part of an employee's retirement package," says California Polytechnic University Professor Joseph R. Blasi. No longer will workers be able to rely on their company for a set pension income, come what may, during their sunset years. Says Frederick M. Rumack, consultant with Buck Consultants Inc.: "The more the retirement nest egg is tied to the company's stock, the more people are pushed to do the best they can for the company."

TAX GOODIES. Between the lip of ideology and the cup of reality lies money—cheap money. An ESOP is a low-cost employee benefit. PPG Industries Inc., for one, expects that using an ESOP to fund stock contributions to its existing profit-sharing plan will cut costs by 30%. The savings largely come from a package of tax goodies. Typically, a company borrows to buy stock for its ESOP. It gets to deduct interest payments and, in a

roundabout way, principal payments as well. Lenders charge companies less for the borrowed money since they get taxed on only 50% of the income they receive on ESOP loans. U.S. West Inc. borrowed \$450 million at a mere 8% to fund its expanded ESOP. Dividend payments on stock held by an ESOP are also deductible, just like interest.

Increasingly, ESOPs are used to supplement or even replace an existing retirement program. Indeed, the ESOP is the latest installment in Corporate America's scaling down of defined-benefit pension plans in favor of defined-contribution plans, which are simpler and cheaper. The most popular is the 401(k) plan, a tax-sheltered account that lets employees set aside a percentage of their pretax salary with the employer matching the worker's contribution.

AN ESOP MAKES PENSIONS MUCH MORE UNCERTAIN

1 An employee starting a new job that pays \$40,000 a year, and getting 5% raises until retiring at 65, can count on these pension amounts under a conventional defined-benefit plan that a company funds with cash:

Years of service	Yearly pension
10	\$7,334
20	23,894
30	58,381

Pension plan formula: 1.3% of final five-year average pay times years of service

2 But if the company instead contributes its own shares in an ESOP, pension amounts will be skimpier if the stock performs poorly, higher if it's a market star and the employee is a long-timer

Years of service	ESOP's total return*	
	4% yearly	12% yearly
10	\$3,627	\$5,149
20	11,278	24,378
30	26,319	89,377

Pension plan formula: Company contributes stock equal to 5% of pay annually through ESOP

*Dividends plus price gains

DATA: HEWITT ASSOCIATES INC.



Now, ESOPs are looming as the cheapest form of defined-contribution plan. U.S. West began its ESOP as part of a 401(k) savings plan because of the cost savings from deducting dividend payments, says Treasurer James T. Anderson. The telephone company pays out some 60% of its annual profits as dividends, and employees will shortly get 14% of the payout.

An ESOP can meet other company objectives, too. Ralston Purina Co. traditionally matched 50¢ on the dollar (up to 6% of salary) of an employee's contribution to its savings plan. Employees could put their pretax money into Ralston stock, a money market fund, or other investment vehicles. Last November, the company converted its plan to an ESOP funded with \$500 million in converted preferred stock. Now Ralston matches 401(k) contributions only with Ralston preferred. But it boosted the match from 50% to 100% to accomplish another corporate goal: pay retiree medical benefits. Ralston is phasing out its subsidy for future retiree health costs. But employees can tap their ESOP at retirement to buy into Ralston's group health plan.

SINCERE MOTIVES? A popular concept is to tie an ESOP to a "productivity" standard. For example, workers at PPG Industries can shelter up to 16% of their gross earnings in the company's savings plan. PPG matches up to 6 points of that 16% through its ESOP. But how much stock employees get depends on



company's return on equity (ROE). On a large scale, PPG contributes the full 6% ROE is 20% or above, for instance, and only half as much if ROE is 11% or less. The carrot could work in many cases. But success is not preordained. Some managers, while wrapping their actions in the mantle of "people's capitalism," are abusing tax-advantaged ESOPs to entrench themselves in power. Others want to tie employee compensation to performance but aren't willing to put in the work," says Polytechnic's Blasi. "Ownership is not an elixir that works wonders on employee productivity. The change, many experts say, is management's willingness to actively involve new owner-workers in decision-making—anathema to many executives.

SECRET BALLOTS. "If people think improved productivity just takes giving prizes to employees, they're wrong," says Joseph V. Vittorio, chairman of PPG Inc. "A big part of my time is spent negotiating with employees." Through a \$7 billion leveraged buyout in 1987, an ESOP owns most of the stock on behalf of 12,500 workers. After years of change-of-control hands, the new setup seems to be working. Avis is paying off its \$400 million of LBO debt twice as fast as scheduled. As a result, consultants valued the company's stock at \$15.47 per share in November, triple the previous year. The law can't make managers pay attention to workers. But employees are getting such hefty minority stakes in

blue-chip companies that managers could be forced to listen. Federal law says public company employees must have voting rights on the ESOP stock they own. It typically takes 4 to 10 years for the ESOP stock to be allocated to individuals. And for the many Delaware-chartered companies, an ESOP is an allowable antitakeover defense only if employees can vote ESOP shares with secret ballots. Disgruntled employee-owners then can safely vote in favor of a raider.

**'ESOPs make capitalists
out of people, but
there's no guarantee
they'll do well'**

The corporate *perestroika* is even sweeping some of the oldest bulwarks of employee participation. Procter & Gamble Co. has had a profit-sharing plan since 1887, and as recently as 1988, its shareholders sided with management and voted down a proposal to let employees vote their 14% stake held in the profit-sharing trust. But last month, P&G moved to create a \$1 billion ESOP which will boost employee ownership to 20%. And since they could vote their ESOP shares anyway, the company went further, allowing them to vote their trust

shares, too. Says a P&G spokesperson: "One of the results of the ESOP is that employees will have a greater voice in the conduct of company business."

Why not? After all, in many companies, an employee's future wealth can vary a lot depending on how the company's stock performs (table). Mouth-watering returns reward the long-time employee with a strong stock. But the nest egg can be frightfully small if the stock gains at only, say, a mediocre 4% pace. Fortunately, the stock of most public companies that adopt ESOPs tend to do at least that well over time, and those companies also fund other retirement plans. Also, the law gives workers the option, at age 55, of starting to diversify out of 50% of their ESOP stock. Still, a hefty chunk of the retirement package could be tied to company stock. Says Robert Rice, partner in the law firm Milbank, Tweed, Hadley & McCloy: "ESOPs make capitalists out of people, but there's no guarantee they'll do well."

Back in 1862, Congress passed the Homestead Act to encourage owner-farmers. In 1974, Congress created, in effect, an industrial homestead act with the ESOP. The ESOP movement could well boost productivity in the 1990s. But, as the original homesteaders learned, the law alone can't assure a bumper crop.

By Christopher Farrell in New York, with Tim Smart in Washington, Zachary Schiller in Cleveland, and bureau reports

THE ODD COUPLE CHASING NORTHWEST AIRLINES

Checchi and Wilson are old hands at corporate dealmaking



CHECCHI: HE EARNED RESPECT AS A TOP STRATEGIST FOR THE BASS BROTHERS

They're not your name-brand takeover artists. But Al Checchi and Gary L. Wilson are bound to become better known in the weeks ahead. They first met 24 years ago, when Checchi was a 16-year-old sophomore at Good Counsel High School in Wheaton, Md. Wilson, fresh from the Wharton school, worked for a financial consulting firm headed by Checchi's uncle. Their lives have been intertwined ever since, from dealmaking days at Marriott Corp. to the Beverly Hills homes they own across the street from each other.

Now, *BUSINESS WEEK* has confirmed, Checchi, Wilson, and their group hold a 4.9% stake in NWA Inc., the holding company for Northwest Airlines Inc., and are believed to have proposed a leveraged buyout. The airline, which also received a \$2.7 billion bid from Los Angeles financier Marvin Davis, has so far resisted all offers.

WHITE KNIGHT? But for Checchi, who earned respect as a top strategist for the Bass brothers, and Wilson, Walt Disney Co.'s chief financial officer, the NWA bid represents a dealmaker's reunion.

Sources close to the group say Wilson

is a passive investor who holds a small equity stake in Checchi's group, and Disney denies any involvement. Wilson has been in Europe overseeing arrangements to raise \$2 billion for Disney to build a theme park outside Paris. But he was an NWA director from May, 1987, to November, 1988, and played a key role in opening talks between Checchi and NWA Chairman Steven G. Rothmeier. And with Davis waging a proxy fight, the Checchi group could emerge as a white knight. Checchi declined comment, and Wilson couldn't be reached.

Checchi and Wilson have been collaborating since 1976, when Wilson, then Marriott's treasurer, hired Checchi out of Harvard business school. At Marriott, the two built the company up by aggressively selling hotels off to private investors and then managing them.

The association contin-

ued after Checchi joined the Basses as top aide in 1982. Two years later, Checchi and Wilson brought together Si Bass and Marriott Chairman J. W. Marriott Jr. in an unsuccessful attempt to buy Conrail. When Checchi helped Bass buy a 25% stake in Disney in 1984, Checchi joined Disney as a Bass emissary. Wilson came on board at Disney as chief financial officer 10 months later. He was a leading candidate even before Checchi urged his hiring.

The two are an odd couple. The 48-year-old Wilson, a running back for the 1960 Duke University football team that went to the Cotton Bowl, is tall and usually reserved. Checchi, smaller and hyperkinetic, talks rapidly and is given to lengthy philosophical discussions. Since leaving the Bass organization in 1980, the 40-year-old Checchi hasn't done many deals. Last year he worked on a blue-ribbon panel set up by Los Angeles Mayor Tom Bradley to study the city's long-range problems. A liberal Democrat, he contemplated running for office. **GOOD MATCH.** Meanwhile, at Disney, Wilson established a strategic planning unit that paved the way for acquisitions of television station, hotels, and a mail-order business. He has expanded the company's use of limited partnerships to finance its films, raised \$723 million by selling the rights to future royalties from Disney's Tokyo theme park, and crafting an elaborate scheme to finance the Paris park with foreign debt and equity placements.

Disney has been equally good for Wilson: Last year, on top of his \$500,000 salary, he was paid a \$550,000 bonus and exercised \$10.7 million in stock options. That gave Wilson more than enough money to join Checchi's group.

For Checchi, the NWA deal marks a return to big-time dealmaking. Using the millions he made with the Bass brothers, he has set up a Century City investment firm that will soon number more than a dozen people.

Checchi's reemergence means more deals are likely to be on the way. It is less clear whether Wilson will always be a partner. But after 25 years of a friendship built on the thrill of making deals, you can be sure that some of Checchi's visits to his neighbor across the street will involve more than a cup of sugar.

*By Ronald Grover
Los Angeles, with Leah
Nathans in New York and
Seth Payne in Washington*



WILSON: WHEELING AND DEALING AT DISNEY

WALL STREET FALLS IN LOVE WITH 'SOFT DOLLARS'

And as their use mushrooms, so does the potential for abuse

If information is the most precious commodity on Wall Street, then "soft dollars" may well be the coin of the realm. Money managers will spend more than \$1 billion in soft dollars this year to get anything from stock-quotation terminals to electronic data bases to consultations with economists. In a stock market with lackluster trading volume, soft dollars are growing fast—rapidly becoming one of the most controversial practices on the Street.

As far as their use mushrooms, so does the potential for abuse. Today money managers can choose from an array of more than 700 investment products—and they don't have to wait until they've generated enough commissions to pay for them. Soft-dollar brokers, in effect, extend credit to their customers, the money managers. The brokers pay the suppliers with hard dollars. And the money managers pay back the brokers by trading securities through their companies. As a rule of

Soft-dollar brokers have, in effect, "unbundled" research, and they staunchly defend the practice. The beauty of the system is that money managers can choose what's most useful to them. "Soft dollars allow you to get research" on companies that the big Wall Street firms don't cover, says Ronald H. Hoenig, president of Hoenig & Co. Donald C. Potts, president of Capital Institutional Services Inc., says the success of soft-dollar brokers during an industry slump attests to the practice's merits. **MUCH LEEWAY.** More than a few money managers, however, are reluctant to talk about using commissions that come out of clients' accounts to buy investment products for themselves. Scott M. Black of Delphi Management Inc. steers clear of the practice. "The business is profitable enough," he says. "I think it's an abuse to pay for your Quotron with your client's commission dollars." The Securities & Exchange Commis-



Soft dollars start with the hard dollars brokerage commissions. Until the 1970s commission rates were fixed, brokers could not compete by pricing. So they lavished all sorts of research on money managers to win their business. When fixed commissions were slashed, many firms failed. This left analysts out of work and money managers short on research. Enter the soft-dollar brokers. They figured out how to get the two together: Order up research a money manager wants, and then part of the money manager's stocking commissions to pay for it. The portion of the commission that goes to suppliers is called "soft dollars." So far, so good. But over the years, some brokers and money managers tried to use soft dollars to cover things far afield from research, such as a firm's rent or advertising. If you stretch the practice too

far, brokers credit money managers one soft dollar for every two hard dollars they spend on commissions. And the soft-dollar brokers generally charge no higher rates than others. **THICK BOOK.** The business is attracting more big players. "It represents one-third of the [institutional brokerage] business, so you can't afford not to do it," says an executive at a major brokerage firm. Citicorp owns Lynch, Jones & Ryan, one of the largest soft-dollar brokers. Equitable Life Assurance Society owns Autranet Inc., whose catalog of offerings is as thick as a telephone directory. McGraw-Hill Inc., publisher of *BUSINESS WEEK* and owner of Standard & Poor's Corp., a widely used supplier of investment information, operates its own soft-dollar brokerage firm. This allows customers to purchase S&P's investment products through trading commissions.

tion gives investment managers a lot of leeway in choosing what to buy with commissions, but any such purchase must somehow enhance the investment process. And in most cases, it does. The SEC gave the soft-dollar business a big boost in 1986 when it approved purchases of computer hardware. Richard G. Ketchum, director of the SEC's Market Regulation Div., says the practice promotes competition by allowing smaller investment managers access to research that otherwise only the biggest might get. Yet soft dollars have been known to pay for junkets with dubious investment value. Research seminars and trips are O.K. only if managers pay travel and lodging out of their own pockets. "Many money managers play fast and loose with soft dollars," says James D. Wright, chief investment officer of Banc

One Asset Management. "We document everything. If the SEC sends an auditor around, I want everything in order." For example, he uses soft dollars to pay for charts used to track stocks. "But if we use those charts for a newsletter, that's marketing, and we allocate that part of the cost to our own hard dollars."

AFTER GRAVY. Wall Street pros say that while excesses of the past have been largely wrung out of the system, some abuses probably remain. One New York brokerage executive, looking for a tenant, says a money manager asked if he could rent space with soft dollars. And on Apr. 11, Charles L. Lerner, associate director of enforcement in the Labor Dept.'s Office of Pension & Welfare Benefit Administration, confirmed that his office is investigating a money-management firm for improper use of soft dollars to paper over trading losses.

Although regulators are looking for soft-dollar abuses, as a practical matter the job falls to pension-plan sponsors that hire money managers. "We've been educating clients about soft dollars," says Edward D. Loughlin, senior vice-president of SEI Corp., a pension consult-

One money manager asked a New York broker if he could rent office space with soft dollars

ing firm. Rather than discourage the practice, however, plan sponsors want some of the gravy. They're telling their money managers to trade through soft-dollar brokers who, in turn, pay for the plans' custodial, actuarial, and consulting expenses.

Executives at many full-service brokers complain that the practice is crimping stock-market liquidity. Soft-dollar brokers offer execution services only. They don't "position" stocks—that is, put their own capital at risk to buy a customer's unwanted shares. The big brokers say that positioning, which adds liquidity to the market, is a money-losing service they offer clients in return for a shot at the easier, more profitable trades. Many of those trades, they contend, now are going to soft-dollar brokers (BW—Mar. 27).

That argument isn't gaining much sympathy. Wall Streeters, after all, vote with their feet. These days more and more, those feet are heading toward soft-dollar brokers.

By Jeffrey M. Laderman in New York,
with Tom Smart in Washington

MARKETS & INVESTMENTS

THE SEC CASTS A NET AT PENNY STOCKS' BIGGEST FISH

Denver's Stuart-James is charged with fraudulent trading

It's nice work if you can get it. A penny stock broker rounds up stock en masse from customers and, without breaking stride, turns around and pushes the same issue on a different bunch of investors. None of the clients, however, hear about the point of the furious buying and selling: fat, juicy, risk-free markups for the firm, which can reach as high as 200%.

That, says the Securities & Exchange Commission, is what Denver-based Stuart-James Co. would do. In its most significant case since announcing a crackdown on penny stock abuses last fall, the SEC said on Apr. 10 that it has filed fraud and deceit charges against the firm, Chairman Stuart Graff, and President C. James Padgett.

LOCKED-IN PROFITS. Graff and Padgett aren't exactly newcomers to the rough-and-tumble world of penny stocks. In 1982, Padgett was suspended from his supervisory post at a Los Angeles penny stock firm for six months by the National Association of Securities Dealers, the industry's over-the-counter cop. And both men worked for Meyer Blinder, the doyen of the business, who heads ailing Blinder, Robinson & Co. Graff and Padgett started Stuart-James six years ago, and last year, with 50 offices in 22 states, it became the largest penny stock firm in the U.S. (table).

The charge of "undisclosed excessive markups" stems from the 1986 underwritings of Find SVP Inc., a New York newsletter publisher, and UMB Equities Inc., a Milwaukee-based investor in medical buildings. No charges have been filed against the companies. The SEC says Stuart-James sales agents were ordered to line up customers who agreed to buy the stocks at low initial offering prices. They also consented to sell the issues back to Stuart-James, at a locked-in profit, after they began trading in the secondary market. Next, the firm's brokers were instructed to resell the stock to new buyers at a price set by Padgett

and Graff—fabulous markups and a markup in excess of 10% aren't necessarily illegal, but the alleged failure to disclose an orchestrated "flipping" arrangement such as the one used in the offerings would be, says Robert M. Feld, the SEC's regional trial counsel.

Graff and Padgett weren't available for comment, but Marc Geman, Stuart-James's counsel, says there were no unfair markups. "We sold stock at the be-

BIG PENNY STOCK FIRMS ARE FEELING THE HEAT

Stepped-up pressure from state and federal regulators is making it harder to make big money—or survive.

Firm	Brokers	Event
STUART-JAMES Denver	1,300	SEC charges fraud, excessive markups
POWER SECURITIES Las Vegas	1,200	NY Attorney General charges fraud, manipulation. Closes voluntarily on Feb. 12
INVESTORS CENTER Hauppauge, NY	900	SEC finds net capital problems. Agrees to liquidate on Mar. 7
BLINDER ROBINSON Denver	850	IRS raids firm in November, 1988. Continues decade-long battle with SEC

DATA: BW

NASDAQ offering price," Geman says. "We don't know what benchmark [the SEC] is using." He also denied that the firm engaged in any deceptive or fraudulent practices. If Stuart-James is found guilty, the SEC could revoke its license and bar its officials from the securities business. SEC Denver Regional Administrator Robert H. Davenport says only that he will seek "significant sanctions."

Although this is the first time that the office has alleged such widespread violations at a major firm, Davenport says such abuses "are not uncommon." But sure, the case will get special attention in the trade. Penny stock brokering may still be nice work all right, and the regulators have yet to demonstrate that they can stop unscrupulous promoters from getting it.

By Sandra D. Atchison in Denver

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BY GENE MARSH

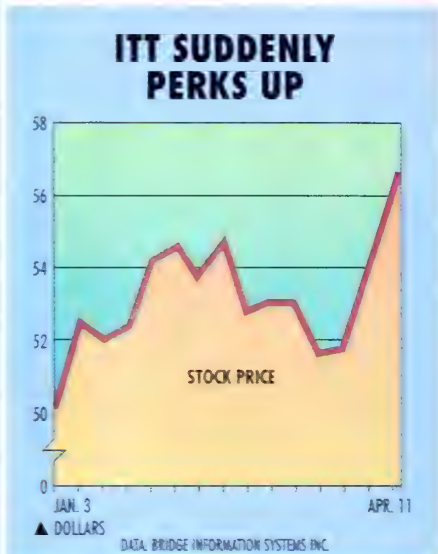
ARE RAIDERS READY TO TAKE ON ITT AGAIN?

In his just-released book, *The ITT Wars*, ITT Chairman and CEO Rand Araskog recounts how he won the bitter battle against raiders Jay Pritzker, Phil Anschutz, and Irwin Jacobs when they tried to acquire the giant conglomerate in 1984. Araskog counsels that managers must accept "both the challenge of hostile raiders and the need to develop creative solutions to current problems." If recent whispers have substance, ITT's management may soon be tested again.

Although no names have yet surfaced, there's talk that a raider group has accumulated a 2% stake. And ITT's long-dormant stock has recently vaulted from 51 to 57 (chart). Despite the rise, it's still way below the breakup value of \$80 to \$100 a share that some asset players say the company is worth. This time around, says one big ITT investor, Araskog may have to make fresh restructuring moves to really boost the shares.

"Araskog has done a super job in making ITT a strong and profitable enterprise," says Jim Awad, president of BMI Capital, who has been buying shares. But, he adds: "Management is much too cautious. It has failed to be aggressive enough in unlocking the great values in the company. That leaves ITT vulnerable to a raid."

'SOLID OPTIONS.' A number of big institutions—which control about 60% of the 133 million shares outstanding—tend to agree. After refocusing ITT by selling more than 100 of its diverse companies, Araskog now has "solid options to bring out ITT's unrecognized values," says the head of an investor group that owns about 1 million shares. He thinks ITT could sell either its 37% stake in Alcatel, a major maker of telecommunications equipment that is 61.6% owned by Compagnie Générale d'Electricité, or Hartford Insurance, which had revenues of \$8.6 billion last year. Other possibilities include the electronics division, which had 1988 sales of \$2.5 billion, or Rayonier, the pulp-and-timber unit that had sales of \$1.2 billion in 1988. The proceeds of any sale could be used to repurchase stock. Since early 1987, ITT has bought back some 12 million shares and is authorized to purchase an additional 5 mil-



lion. Management now owns about 1%.

Awad notes that, strictly on earnings, the stock is way undervalued. ITT earned \$5.41 a share in 1988 and is expected to post \$6.50 in 1989 and \$7 in 1990. Shares now sell for 8.8 times earnings, vs. 12 times earnings for the Standard & Poor's 500-stock index.

Phua Young, an analyst at Shearson Lehman Hutton, says Araskog won't cave in to a raid, but "a further restructuring could happen." ITT spokesman Jim Gallagher says the recent sale of ITT's telephone operations to Metro-media is the last of the asset sales under current plans. But, he adds, since management wants to serve the best interests of shareholders, it will always consider any good offer for ITT's assets. Araskog, however, thinks that ITT now has the core pieces in place for continued long-term growth.

HIGH HOPES FOR A HOME-OFFICE HELPER

Just about everything comes in portable sizes these days. There's the pocket TV, the mini-fax machine, and the laptop computer. Now comes the portable binder, a handy home-office product that has added pizzazz to General Binding, an otherwise prosaic office-equipment maker. Last year investor anticipation of General Binding's \$99 personal binder helped send the stock skyward by 86%.

General Binding's compact One-Step system, introduced early this year, comes with proprietary folders. After papers are stacked inside, a heat-plus-adhesives process permanently binds them into the folder. The machines are

expected to add \$10 million to \$15 million in sales and 10¢ to 15¢ a share to earnings. A plastic loose-leaf binder will be introduced later this year.

General Binding now trades at 28, not far from its 1988 high of 29. But some big investors are betting that the stock is poised to leap again. The reason: Earnings are expected to sustain their torrid 50% annual growth this year and next. Tim Reiland, a partner at securities house Cleary Guil Reiland McDevitt & Collopy, says that if the company achieves its sales and earnings projections, the stock could hit the 35-to-40 range over the next 12 months.

"The company aims to double sales to \$500 million and triple earnings in the next four years by sustaining sales growth of 20% a year," says President and CEO Rudy Grua.

CUMMINS ENGINE ON THE FAST TRACK

Investors who bought Cummins Engine in early December, when the stock was around 48, saw their shares take off: Cummins jumped to a high of 67 in a matter of days. After slipping a bit, the stock is back to its Yuletide high, elevated again by takeover talk and a turnaround in earnings.

Cummins now "appears to be an engine for a win-win situation," says the head of a New York investor group who has been snapping up shares of the world's largest independent maker of diesel engines. He says that if management sustains the profits surge, Cummins stock should step up smartly. But, he adds, if the share price falters, British conglomerate Hanson will buy Cummins. Hanson has been gobbling up U.S. companies and has amassed a 9.8% stake in Cummins. The Federal Trade Commission has cleared Hanson to acquire up to 15% of Cummins' 10.6 million shares outstanding.

"Either way, a target price of \$90 to \$95 a share seems reasonable," figures this investor. He is confident that Hanson, which is believed to have a war chest of \$5 billion, will raise its stake to 15% before long and then seek control. Although Cummins executives have been assured by Hanson that it will be a mere investor, as indicated in Hanson's filing, that filing can be amended. Cummins Chairman Henry Schacht told analysts at a recent meeting that his company intends to stay independent. He added that Cummins expects to post first-quarter earnings of \$1.50 a share, vs. 50¢ a year ago.

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TABLE-TOP FUSION LOOKS LESS LIKE A PARLOR TRICK

Now other groups have achieved similar—startling—results

They've got to be certifiably nuts." That was the initial reaction of James Mahaffey, a Georgia Tech nuclear engineer, when he heard in late March that scientists at the University of Utah had produced energy from a fusion reaction in a bottle. Until then, fusion theory required sun-high temperatures to work. But on second thought, he added: "Either that, or they'll get a Nobel prize."

Mahaffey wasted no time trying to find out which was correct. The day after the Utah announcement, he cajoled four other Georgia Institute of Technology researchers into joining him to try to confirm the possibility of table-top fusion. At scores of laboratories around the world, scientists scrambled to repeat the experiment. They relied on sketchy copies of a scientific paper by Utah's B. Stanley Pons and his colleague, Martin Fleischmann of Britain's Southampton University. The copies quickly crisscrossed the globe, spewing forth from facsimile machines even before the Lausanne (Switzerland)-based *Journal of Electroanalytical Chemistry* could rush it into print.

CHEMISTRY'S WOODSTOCK. On Apr. 12, Mahaffey and many of those scientists gathered in Dallas for the second scientific meeting in two years at which revolutionary data turned scientific theory on its head. Just two years earlier, physicists waited all night to crowd into a special session at the American Physical Society's 1987 meeting, later dubbed the Woodstock of Physics. In that session they heard the first data on superconductors that conduct electricity with no



GEORGIA TECH'S MAHAFFEY: ENVISIONING FUSION-FUELED CARS

resistance at almost room temperature.

At the Dallas meeting of the American Chemical Society—already called the Woodstock of Chemistry—the vast majority of the 9,000 scientists in attendance crowded into a convention hall to hear reports on a technology that may lead to the production of inexpensive electricity from seawater. The extra-added attraction: On the eve of the hastily called special session, two groups at prestigious universities reported they had obtained results that seem to confirm the Pons-Fleischmann experiment.

One of those was Mahaffey's group. Their first attempt, with equipment used in freshman chemistry to split water into hydrogen and oxygen, flopped. "We didn't see a thing," recalls William Livesay, the team's metallurgist. The next

time they were more careful. At 4: p.m. on Apr. 8, just 90 minutes after filling a special quartz-crystal flask with "heavy" water, they detected the first signs of fusion: The gauges on four neutron counters climbed sharply to 600 p.p.h. "I see it, but I still don't believe it," says Livesay. "I just don't understand how or why it works."

Heavy water is composed of a form of hydrogen called deuterium—its nucleus has a neutron along with the usual proton. Submerged in the flask of water, a rod of palladium, a metal with an affinity for hydrogen. Pons and Fleischmann passed an electrical current through the heavy water breaking it down so the deuterium would be attracted to the palladium. The Utah chemists speculate that when deuterium ions are absorbed into the crystalline structure of the metal, they become packed so densely that they fuse, releasing energy.

The Georgia Tech team watched their apparatus run smoothly for almost three days, then announced their results on Apr. 11. That same day, researchers at Texas A&M University reported that they had produced surplus energy in the form of heat—comparable to the fourfold gain claimed by Pons and Fleischmann. The confirmations lend credence to a similar report a few days earlier from Hungary's University of Debrecen. Also, Brookhaven National Laboratory said that it had confirmed the results of a group led by Steven E. Jones, a physicist at Brigham Young University. Jones has been working on "cold" fusion since 1980, several years before Fleischmann and Pons started their experiments.

SAFE INSTALLATIONS. To scientists unfamiliar with Jones's published work, the notion of bottling the sun's fusion for nance smacks of utter nonsense. Atomic nuclei find each other so repellent that they should take tremendous energy—millions of degrees of heat and enormous pressures—to force them to combine. But when fusion does occur, it unleashes far more energy and far less radiation than the fission process at the heart of today's atomic power plants. And a gallon of seawater contains enough deuterium to replace thousands of gallons of gasoline.

If cold fusion turns out to be real, says Mahaffey, "the global implications are just overwhelming—an end to our dependence on oil, for instance." Global warming from burning fossil fuels and the danger of supertanker spills like the one in Alaska could become relics of the past, he explains, "because one of the most exciting things about this is that it looks like it will scale down." That is, he believes that cold-fusion power plants

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DW 252

could be safely installed in homes, factories, and even cars.

That might start to happen before the turn of the century, adds engineer Mahaffey. "Pons said applying the technology would take 10 years. Fleischmann sort of kicked him and said 20 years. But they're not engineers. I think they could be surprised at how fast engineers can swing into action."

However, there are many fundamental scientific questions to settle before Detroit can begin thinking about fusion-powered cars. For the numerous skeptics, the lack of a coherent theory that explains solid-state fusion is probably the biggest stumbling block. But the first glimmerings of such a theory emerged at the ACS special session thanks to a last-minute addition to the roster of speakers. K. Birgitta Whaley, theoretical chemist at the University of California at Berkeley, reported that deuterium belongs to a special class of particles, called bosons, that have certain peculiar properties. Because of these quantum-effect features, the repulsion between nuclei can be blocked inside a crystal, and the deuterium ions can practically sit on each other's lap. As a result, Whaley says, the theoretical fusion rate "is enormous"—much higher than any results yet measured.

DOUBTFUL. Still, many scientists at the ACS meeting remained doubtful, pointing to the failure, so far, of many other laboratories that are attempting to duplicate the Pons-Fleischmann feat. Even Harvard Laboratory, the research arm of Brookhaven's Atomic Energy Authority, has not been able to detect clear evidence of fusion—and Harwell was given a detailed "recipe" by Fleischmann, who is affiliated with the lab, back in February. It has been working on the experiment since early March and now has 12 "Fleischmann cells" operating.

For a while, at least, the researchers working on warm superconductors are basking in relative obscurity. "There's nothing I like better than to see the attention go elsewhere," said Donald Murphy, a researcher at AT&T Bell Laboratories who went to the ACS meeting. "I know what these guys are in for—the phone calls and media attention."

Indeed, on Apr. 11, Fleischmann flew to Southampton to continue his work at a secret location, perhaps in Italy. As for Pons, when one skeptic at the ACS meeting asked if he were "Prometheus, Pandora, or the Piltdown man," he retorted, "No comment." Everyone agrees there is no middle ground. Cold fusion is either the greatest discovery of the century or its biggest scientific fiasco.

By Otis Port in New York and John Carey in Dallas, with bureau reports

Developments to Watch

EDITED BY NAOMI FREUNDLICH

HIGH-TECH PROBE OF OUR ACHING BACK



which says it pays out about \$1 million every working day for costs related to back pain, underwrote a computerized monitor at pinpoint weak muscles that could cause backaches and other injuries. Developed by Dr. Carlo J. Deluca, director of Liberty Mutual's NeuroMuscular Research Center, the monitor could save money in two ways: as a screening device and a way to check the progress of therapy.

The device works much like an electrocardiogram: Six electrodes are stuck on the skin, over the back muscles, where they record electrical signals generated by contractions. Tired or injured muscles produce different signals than healthy ones. Researchers are still learning how to interpret the signals, but in a study of 40 members of the Boston University rowing team, the system predicted with 90% accuracy which athletes either had or were prone to back pain. Another study will follow this year's freshman rowers through graduation to see how good the monitor's predictions are for them.

WILL NEC'S OPTICAL MEMORY PARK A REVOLUTION?

Compared with today's memory chips, which can store up to 4 million bits of computer data on a thumbtack-size slice of silicon, the 1,000-bit optical memory chip recently unveiled by NEC Corp. seems positively primitive. But the Tokyo company believes it could prove just as revolutionary as the first of the conventional 1,000-bit memories developed back in 1970.

That's because the optical chip isn't just a memory. It also processes information—much as an eye does. An image falling on the chip is instantly recorded, and simultaneously processed, by 1,000 light-sensitive picture elements, or pixels. As a result, clusters of the chips may soon find applications in artificial vision for robots, sensors, and image-processing systems—or in a collision-avoidance system for cars.

NEC's new chip is quite different from the imaging chips in a video camera. Its complicated, multilayer sandwich of gallium arsenide and gallium aluminum arsenide can hold an image indefinitely while consuming very little power. Eventually, it could pave the way for superfast optical computers.

TEACHING CELLS TO FIGHT MULTIPLE SCLEROSIS

Multiple sclerosis is an insidious disease, catching its victims in the prime of their lives. Characterized by loss of coordination, weakness, and blurred vision, MS occurs when the body's immune system mistakenly attacks the sheaths that surround nerve fibers of the brain and spinal cord. There is no

cure or specific treatment. But researchers at Brigham & Women's Hospital in Boston have now devised a vaccination that may someday curb this unwanted immune response.

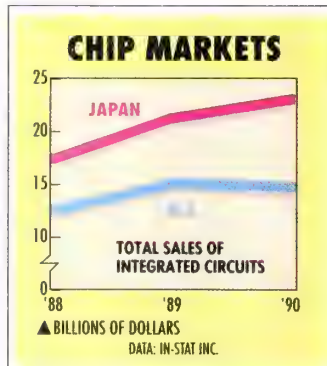
In a small trial, Dr. David Hafler and Dr. Howard Weiner removed T-cells—one kind of immune cell—from the spinal fluid of three MS patients. T-cells are normally not found in the spinal fluid, so researchers believe they might be the cells that attack the nerve sheaths. The team grew more of the cells in the laboratory, rendered them harmless, and then injected each set back into the original donor over a six-month period. Three weeks after the first injection, the doctors detected a suppression of the errant T-cells. In animals, similar vaccines arrested the disease. Weiner cautions that the vaccination is a long way from being a standard therapy for MS sufferers, but he is expanding his study to more patients.

A SURGE IN SEMICONDUCTORS—ESPECIALLY FOR JAPAN

The outlook for semiconductor sales growth has improved markedly since forecasters took the industry's pulse earlier this year. Then, single-digit gloom was the general mood. But In-Stat Inc. has just raised its prediction to almost 19% worldwide, to \$53.4 billion—with integrated circuits doing even better: up a projected 21%, to \$43.5 billion.

That's the good news. The bad news is that the big U.S. chipmakers are on the verge of losing half of their own backyard market, which In-Stat, based in Scottsdale, Ariz., figures will grow 14.5% this year, to \$13.2 billion. For the first time, a Japanese company has edged into the ranks of the top five U.S. chip suppliers. Thanks to a 50% jump in its 1988 U.S. sales, Toshiba Corp. pushed past Advanced Micro Devices Inc. to take over the No. 5 spot—and trim the U.S. market share for big domestic producers to 51%, down from 55% in 1987.

And pressures from Japan are going to do anything but slacken, judging from the investments that Japanese suppliers are pouring into chip-making equipment. The latest numbers from the Semiconductor Equipment Association of Japan show that total capital spending during the first nine months of last year was up 75%.



HOW ALASKA IS CRUNCHING THE OIL-DAMAGE NUMBERS

Scientists tracking the Alaskan oil spill are gathering reams of detailed information on the relentless spread of the oil slick, the death toll among animals and birds, and the water quality at numerous points. To manage this flood of data, Alaska's Environmental Conservation Dept. is using a handy computer tool: a desktop mapping program called GeoREF, from Generation 5 Technology Inc. in Denver. It displays the collated data on digitized maps.

At their nightly meetings, the scientists use the detailed computer maps of the Prince William Sound area to plot cleanup strategy. Scientists expect to continue monitoring the effects of the disaster for years to come. In the longer term, says Marshal Kendziorek, data coordinator for the department, the data and desktop maps will provide a vital record of the environmental impact of America's worst oil spill.

DELL COMPUTER HITS THE DRAWING BOARD

The mail-order clone maker is recasting itself as an innovator

Few entrepreneurs would be unhappy with what Michael S. Dell achieved last year at the ripe old age of 24. When he expanded his mail-order computer business to Britain and Canada, sales boomed. Revenues for Dell Computer Corp., a maker of IBM PC clones, jumped 82% to \$258 million. Net income rose 54% to \$14 million. Dell, a University of Texas dropout, took his company public in June—and his 56% stake was worth \$93.5 million on paper.

But Dell is a little down these days. Rapid success has brought growing pains. As inventories quadrupled to \$104 million in late 1988, Wall Street lost confidence. Since November, the company's stock has tumbled 42% to 7.

Now, with dozens of Asian PC suppliers vying for Dell's price-conscious customers, the five-year-old company is rethinking its strategy. It will still sell by mail order. But it is beefing up its technical skills to be an innovator—like market leaders IBM and Compaq Computer Corp. "He's trying to become a major-league PC player," says Bruce Stevens, an analyst with market researcher International Data Corp.

NEW SCRIPT. The new character in this new script is Glenn Henry, a 47-year-old computer scientist recruited from IBM's nearby Austin (Tex.) laboratory. As senior vice-president of product development, Henry seems to have filled a role vacated by Graham Beachum. A former Tandy Corp. marketing executive, Beachum helped Dell formulate strategy for two years. But he suddenly left his senior vice-president's post a year ago after a falling-out with the boss. The difference is that where Beachum concentrated on marketing angles, Henry is focusing on technology.

The new strategy is no surprise, given the sophisticated customers Dell is attracting. Nearly half of its 1988 sales came from high-end PCs based on Intel Corp.'s 80386 microprocessor. And in February, Dell added its first multiuser computer system, which uses as its basic software the Unix operating system. Henry has still bigger things in mind. He plans to file applications for nine patents and may produce a clone of the IBM

Personal System/2 this year. One of his first acts was to kill an earlier PS 2 clone that Dell announced a year ago but never built. "It had too many parts and the wrong design," says Henry.

Under Henry, who oversaw Big Blue's development program for Unix PCs, the R&D staff has mushroomed to 150 from a

handful a year ago. These engineers are designing custom chips, such as one that saves money by doing tasks that previously required several chips. Dell also is adding software specialists to develop Unix programs. And it's already working on machines based on the new Intel i486 microchip. Henry wants Dell PCs to incorporate advances such as video-quality graphics and natural language programming—before IBM does. His aim: "To build the world's best computer."

That's a tall order for a company that has no patented technology and no history of innovation. Dell has succeeded by establishing a reliable brand name in the otherwise no-name clone business. With his \$7 million R&D budget, Dell is going up against the several hundred million dollars that IBM spends. "It's right to be skeptical," says Daniel C. Benton, an analyst with Goldman Sachs & Co.

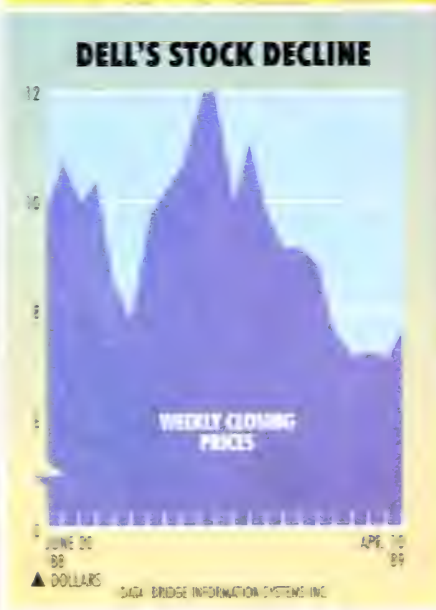
NEXT, DOWN UNDER. Even if Dell's long-range plans are achievable, moreover, the company still has to deal with its financial situation. Last October, only four months after an initial public offering raised \$31 million, the company had no cash. By January it had only \$23 million on hand and short-term debt of \$27 million. "Where did all the money go?" asks Prudential-Bache Securities Inc. analyst Kim Brown.

The answer is plant and inventory. Before the IPO, Dell had been unable to meet demand. Deliveries stretched from 3 days to 35, and an \$18 million backlog built up. Every spare dollar went into expanded capacity. Then, buoyed by high ratings for his machines from computer magazines, Dell overestimated fourth-quarter demand. That led to excess inventory, a problem he now says should be cleared up by July, though Wall Street doubts it. "My focus isn't the stock price," Dell says. "It's building my company." This year, for example, he plans to double capacity.

Dell's growth is expected to slow to about 20% this year. But that may still be faster than the PC industry's. Overseas expansion is the key. Dell expects its sales in Britain to double from last year's \$40 million. Its Canadian operations, opened in October, are still booming. And the company's West German business is starting to break even. The next target is Australia.

Those are just a few of Dell's major-league plans. Eventually, "we'll be one of the top three [personal] computer companies," he asserts, momentarily overlooking his 1.8% market share. It sounds like boasting. But then, nobody expected a kid who once sold mail-order from his dorm room to come this far.

By Kevin Kelly in Austin, Tex.



AN SUN STAND THE HEAT IN THE PC MARKET?

new models pit it against Apple, IBM, and Compaq

April Fools' Day always inspires outlandish pranks by the youthful engineers at Sun Microsystems Inc. One year an executive's Ferarri was propped perilously above a building near Sun's headquarters. This year's gag had a special edge: As engineers put the finishing touches on a line of eight new computers, pranksters draped sheets of plastic, summoned extortor trucks, and started up smoke machines—to feign a fumigation of "bugs" in the machines.

The point was clear to everyone at Sun: The seven-year-old company has a great deal riding on its new products, and it can't afford to make any mistakes. The new computers, introduced on Apr. 12, will take the Mountain View (Calif.) company more directly in the path of personal-computer giants such as Apple, IBM, and Compaq. The move also will test Sun's abilities as a high-volume manufacturer and determine whether computers based on its Sparc microprocessor can become major contenders in the battle for office sales.

SPILLED WATER. That could be enough to challenge any company—let alone a highflier whose sales are expected to soar to about \$1.9 billion, the fiscal year ending in 1990. But Sun has even more to contend with. As the company broadens its product line, Digital Equipment, Hewlett-Packard, and IBM are moving in on its stronghold: the market for higher-priced workstations sold to engineers. Wall Street is already asking whether Sun can handle these challenges. The stock has dropped from 21 last February to 16 recently, despite an expected jump in profits to \$118 million for the fiscal year. Says President Scott G. McNealy: "Our cup is overflowing, but let's see it as spilled water."

The key to changing that perception will be big sales of a new entry-level workstation, dubbed Sparcstation 1. The machine will help move Sun into such markets as technical publishing and in-

ventory management—a logical leap from its current role in engineering design and software development. At \$8,995 for a basic model and \$15,495 for a fully equipped version, the new Sun machine runs up to five times as fast as comparably priced machines from Apple Computer Inc. or IBM.

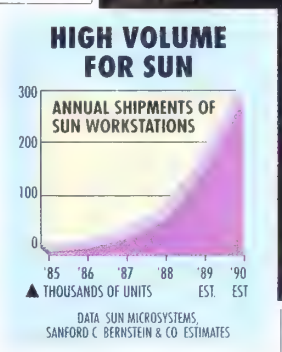
The lower prices should open new markets. On Wall Street, for example, Sun's \$40,000 workstations have been slowly adapted for trading. The new, cheaper model can display data in three

workstations. That means the company must convince independent software developers that its workstations will sell in sufficient volumes—at least 250,000 units annually—to justify writing for Sun. To put that in perspective, in its entire history Sun has sold only 150,000 machines.

RUNNING FREE. How well Sun succeeds with the Sparcstation 1—and lower-priced systems due out in 1990—will help determine the fate of the company's basic strategy. These are the products that can build up volume for Sparc, the microprocessor that Sun introduced nearly two years ago. McNealy's plan is to make Sparc technology, rather than Motorola Inc.'s or Intel Corp.'s, the standard for Unix-based workstations. In addition to boosting sales, that would let Sun run free of the other chipmakers instead of waiting for new versions of their chips to improve the performance of Sun's machines. But so far, Sun has sold only 6,800 Sparc-based systems.



BECHTOLSHEIM AND HIS "PIZZA BOX" COMPUTER



windows on one screen and at the same time do all the analytical work PCs now do. "Sun now becomes more economically justifiable because it can do both analytics and trading," says W. Leo Hoarty, a systems vice-president at PaineWebber Inc. Vicki J. Brown, an analyst at International Data Corp., figures the new machine can also function as the main computer for a work group or small department. Some 230,000 such machines using Unix are now sold each year, IDC estimates.

Still, making Sun's high-volume strategy work will take some doing. First, suppliers of office software must be persuaded to adapt their programs for Sun's version of Unix, the basic software, or operating system, used on its

About 75% of its sales are from machines based on Motorola or Intel microchips.

Sun knew two years ago that low-cost models would be the key to making Sparc fly. So it set up a five-member team headed by co-founder Andreas V. Bechtolsheim, the German-born engineer who designed Sun's first workstation as a Stanford University student. The team produced what analysts call an elegant workhorse, as strong as a mainframe—about the size of a pizza box. "This is the beginning of a strategy to take over the desktop," says IDC's Brown. How's that for an advertising slogan: a pizza box on every desk.

By Jonathan B. Levine in Mountain View, Calif.

TAIPEI

The hot word in trade shows.

	Taipei Int'l Electronics Show	1989 Oct. 13-19
	Taipei Int'l Gift & Stationery Autumn Show	Oct. 26-30
	'89 Taipei Fashion Week	Nov. 9-13
	Taipei Int'l Furniture & Woodworking Machinery Show	Nov. 21-25
	Taipei Elec	1990 Mar. 1-5
	Taipei Int'l Food Industry Show	Mar. 12-16
	Taipei Int'l Gift & Stationery Spring Show	Mar. 23-27
	Taipei Int'l Industrial Machinery Show	Apr. 6-12
	Taipei Int'l Sporting Goods Show	Apr. 20-24
	Taipei Int'l Cycle Show	Apr. 20-24
	Taipei Int'l Footwear & Leather Goods Show	May 3-7
	Taipei Int'l Auto Show	May 14-18
	Taipei Int'l Home Improvement & Houseware Show	May 25-29
	Computex Taipei	Jun. 6-12
	Taipei Int'l OEM/Subcontracting Show	Jun. 21-25
	Taipei Tech	Jun. 21-25
	Taipei Import Fair	Aug. 30-Sep. 5
	Taipei Int'l Jewelry & Timepiece Show	Sept. 14-18
	Taipei Int'l Toy Show	Sept. 26-30
	Taipei Int'l Electronics Show	October Oct. 26-30
	'90 Taipei Fashion Week	

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HOW TWO BIG GROCERS ARE BRINGING HOME THE BACON

one, an LBO that works. For another, a promising merger

a mundane sort of business, supermarkets certainly attract a lot of -powered, high-priced attention. Apr. 10 announcement that a p led by Salomon Brothers Inc. ld acquire Grand Union Co. for e-billion was just the latest in a e-year wave of dealmaking that transformed the industry. In Cali- ia alone, four out of the top five ery chains have changed hands or e private. Here's a look at how two hese deals are faring.

SAFEGWAY: IT'S FOUNDFINDING CRITICS

On a business trip to Australia, Peter A. Magowan passed up sightseeing to prowl the aisles competitors' supermarkets for new s. The chairman of Safeway Stores also likes to visit his own stores nounced, and managers had better e sure there are no long waits at the kout counter. "If I see lines," he s, "I get angry." agowan's single-mindedness has red the Oakland (Calif.) grocery chain since its \$5.7 billion leveraged out by Kohlberg Kravis Roberts & in 1986. Critics warned that the debt

would cripple Safeway, but Magowan has proved them wrong.

Since the buyout, he has updated stores, cut costs, held wage rates down, and sold off lagging units. The new company surprised analysts by turning its first profit last year, earning \$31 million on \$13.6 billion in sales. That's 69% of pre-LBO sales in only half as many stores. Its operating margin was 4.5% in 1988, slightly ahead of other large chains. And it has slashed debt in half, to \$3.1 billion, thanks to the high prices it got for the 1,182 stores Magowan sold. "Safeway is the best LBO success story in the retail food industry," says analyst Gary M. Giblen of Rotan Mosle Inc. in Houston.

Now that the fat is cut, however, Safeway has to prove that it can sell groceries as well as it sells real estate. No one is more aware of that than Magowan, whose father built Safeway into a powerhouse in the 1960s. Peter Magowan, 47, is credited with turning the chain around in the 1970s by cutting costs and sprucing up stores. But to

elude a takeover attempt by Dart Group Corp., Magowan agreed to a buyout with KKR.

The LBO debt has forced Safeway to slash capital spending in half, to about \$300 million annually. But the chain has still managed to remodel more than 100 stores a year. These makeovers, at an average of \$750,000 apiece, raised store sales by 20% to 100% or more. The stores offer some 300 produce items, up from about 100, and goodies such as fresh-squeezed orange juice. Says Gary G. Michael, vice-chairman of competitor Albertson's Inc. based in Boise, Idaho: "They've competed very vigorously."

SUPERSTORE PUSH. Safeway still has some weak spots, though. Since 1986, for example, Giant Food Inc., based in Landover, Md., has gained six points of market share in Washington, D. C. Half of that has come out of Safeway's hide, says analyst Susan Spielberg of Shearson Lehman Hutton Inc.

Nor has Safeway been able to keep pace in new-store openings, and smaller competitors with less debt are rushing to take advantage. While it's less than half Safeway's size, for example, Albertson's opened 44 stores in 1988 to Safeway's 22. Now, Safeway plans 30 new stores this year and 40 in 1990. All will be "superstores," 40,000-square-foot emporiums full of high-margin delis, bakeries, floral shops, and video rentals. One idea being tested: Service Village, a kiosk offering shoe repair, key-cutting, fax machines, and other services.

Safeway may even swallow up some competitors. Magowan has bid on several small chains in the past two years. He was outbid on all but one, a 17-store Canadian chain. But at least now, as he combs rivals' aisles, Magowan is shopping for a lot more than ideas.

By Robert D. Hof in Oakland, Calif.

SAFEGWAY

Ownership: Kohlberg Kravis Roberts	
1988	Dollar figures in millions
REVENUES	\$13,600
OPERATING PROFIT	\$325
LONG-TERM DEBT	\$2,800
STORES	1,144
STATES	18

DATA: COMPANY REPORTS, BW



CHAIRMAN MAGOWAN: STORE MAKEOVERS INCLUDE OFFERING MORE FRESH PRODUCE

AMERICAN: CAN IT MINE LUCKY STORES' MAGIC?

Sam Skaggs comes from a long line of empire builders. An uncle founded Safeway Stores Inc., and Sam's father was on his way to building the nation's largest drugstore chain when he died in 1950. Taking up where his father left off, Skaggs used a string of acquisitions to build American Stores Co. into an \$18.5 billion company, with

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17 food-and-drug stores in 39 states. For a while, though, it looked as if the year-old Skaggs might lose his biggest prize. Last June, American announced the \$2.5 billion purchase of Lucky Stores Inc. But the California Attorney General tried to block the move on antitrust grounds. After five months, American won tentative approval for the merger on Mar. 31. By buying Lucky's 352 stores to his own 216-store Alpha Beta Stores Inc. chain, Skaggs will become the biggest player in the \$14 billion Southern California market. A federal judge could yet order Skaggs to divest some or all of Lucky. But for now, the company's biggest concern is revitalizing dog-eared Alpha Beta. The stores are widely criticized for their shabby appearance, poor service, and high prices. Lucky, on the other hand, has carved out a niche as Southern California's self-proclaimed low-price leader." With roughly the

same number of stores, Lucky has captured 16% of the regional market—nearly double Alpha Beta's share.

You almost wonder who took over whom. Alpha Beta will disappear, with all the supermarkets taking the Lucky name, and Skaggs hopes Lucky's low-cost, high-efficiency operating style will rub off, too. Lucky offers few frills, but it gets shoppers in and out of stores fast. It opens a new checkout line if more than three customers are waiting, puts cash registers at its deli and bakery counters, and encourages people to pay with automatic teller machine cards. Lucky boasts an operating margin of 4.7%, while Alpha Beta's 2% margin is far below the industry's 3.9% average. "They just need to spruce up their stores a bit and be given a more consistent marketing plan," says Larry Del Santo, the president of Lucky, who will become chairman of the combined units. "We'll try to give them some as-

pects of the higher level of service that we have gotten a reputation for."

Lucky's magic comes at a hefty price, though. Seven months' interest on \$2.1 billion in acquisition debt already cut American's earnings last year by 36%, to \$98 million. And Skaggs plans to spend more than \$500 million over the next three years to build as many as 20 new stores a year, renovate the old Alpha Betas, and expand as many as possible to at least 35,000 square feet from the current average of 23,000 square feet.

While the chains expect to save some \$70 million a year by combining advertising and distribution, the heavy debt and ambitious capital-spending plans could leave Skaggs with little room to maneuver—especially if price wars erupt. Even before the merger, Alpha Beta's prices were the second-highest of seven chains ranked by the California Public Interest Research Group. Del Santo vows to bring Alpha Beta's prices quickly down to Lucky's level. To keep costs down, the combined stores will offer few extras besides bakeries, delis, and some specialty counters. It works for Lucky, and with any luck it will work for Lucky's new parent, too.

By Ronald Grover in Los Angeles

AMERICAN STORES*

Ownership: Public company 11% owned by Sam Skaggs

1988 Dollar figures in millions

REVENUES	\$6,200
OPERATING PROFIT	\$178
LONG-TERM DEBT	\$3,100**
STORES	568
STATES	2

*Alpha-Beta and Lucky supermarkets only

**Corporate DATA: COMPANY REPORTS, BW



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WHO SAYS PENGUINS CAN'T FLY?

They're finally in the Stanley Cup Playoffs—and in the black

The Pittsburgh Penguins once set a standard for futility in professional sports. Created as an expansion team in 1967, the hockey franchise posted 20 straight years of financial losses, filed for bankruptcy once, went through more owners than Casanova went through mistresses, and won barely a third of its games.

You wouldn't know it to see the Penguins—or the balance sheet—these days. With a youthful team built around its star center, league-leading scorer Mario Lemieux, the Penguins are a resounding success. The tickets you once couldn't give away are now often scalped at up to \$100 apiece—four times the box-office prices. Of the 40 regular

season home games in the 16,025-seat Civic Arena, 34 were sold out. At Westinghouse Electric Corp., for example, executives who want to entertain clients now jockey for seats in the company's box. "The presence of Mario Lemieux has created a tremendous interest," says G. Reynolds Clark, a Westinghouse manager. Season subscribers now make up 61% of ticket sales, up from 19% five years ago, before Lemieux arrived.

RUSTY BLADES. Best of all, for the Penguins and owner Edward J. DeBartolo Sr., the team is now not only in the Stanley Cup Playoffs for the first time in seven years but it also has knocked off the New York Rangers in four straight games. Failing to make the



LEMIEUX LEADS THE NHL IN SCORING

playoffs six years in a row is hard to do since only 5 of the 21 teams in the National Hockey League don't qualify. And the extra, post-season games, with little addition to player costs, often make the difference between a profitable and an unprofitable season. For the Penguins the playoffs mean up to \$200,000 in profits per home game.



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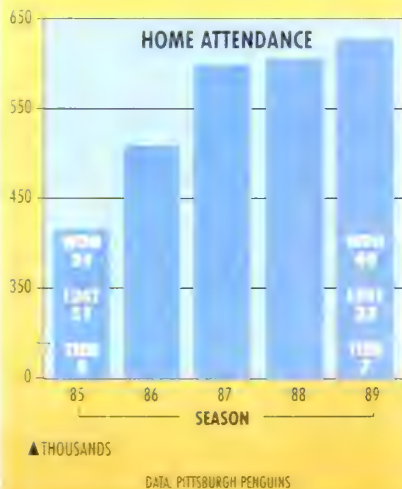
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earlier years the team was so anxious to make the playoffs that the front office mortgaged its future to get in. Management routinely traded away promising future draft choices for seasoned players with just enough "legs," they say in hockey, to stumble into the year's playoffs. Eventually, the Penguins not only missed the playoffs but wound up with a team composed of aging players who couldn't keep up. In the 1983-84 season the impotent Penguins won only 16 games and lost 58. Home attendance averaged only 6,800 a game. The franchise lost \$3.9 million.

DeBartolo, a billionaire shopping-mall developer who in 1978 had the Penguins more or less dumped in his lap when the previous Penguins owner gave him the team to pay off a debt, initially let the team drift. But as one league official ribbed him: "He has a big ego, and he doesn't like to lose—even in hockey." He also has been goaded by his son Richard Jr., owner of the National Football League's three-time champions in the decade, the San Francisco 49ers.

THE CHECK. Whatever the reason, the DeBartolo in 1984 reversed the earlier approach. He gambled on a three-year, \$575,000 contract that included a \$100,000 signing bonus to grab Lemieux, 18. Despite his impressive junior

FANS LOVE THE LEMIEUX ERA



league scoring records, Lemieux had a long way to go to achieve the superstar status of Wayne Gretzky, then of the Edmonton Oilers. In 1987, DeBartolo traded to obtain established megastar Paul Coffey, the top defenseman of the Oilers, to complement Lemieux. A year later he traded again, for virtuoso goalie Tom Barrasso.

The result: After losing \$22 million

over the past decade, the franchise is expected to post its second straight year of profits this season, some \$2 million on a 16% rise in revenues, to \$13 million. Still, DeBartolo must dig deeper into his wallet. Last year Lemieux demanded a raise after the Los Angeles Kings lured Gretzky away from the Oilers with an eight-year contract paying a shade under \$20 million. Lemieux won a single-year raise of 166%, to about \$1.6 million, even though his contract wasn't up for renegotiation. But to keep the Pittsburgh star after the 1990-91 season, DeBartolo undoubtedly will have to match the lush Gretzky contract.

That's for starters. Tony Esposito, the former Chicago Blackhawks goalie who became the Penguins' general manager last year, has a virtual blank check from DeBartolo to use in shopping for talent. "I want to build a formidable team," says DeBartolo. But there's a problem. With the Penguins playing before virtually a capacity crowd every night, the regular season offers little opportunity to achieve the revenue growth necessary to cover the blank check. Lemieux and company will have to become annual participants in the playoffs if DeBartolo is to turn the team's financial follies into a distant memory.

By Gregory L. Miles in Pittsburgh

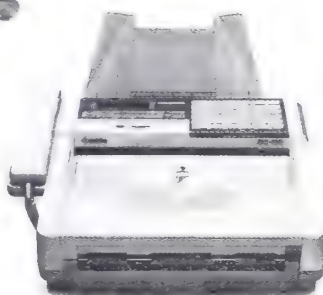


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HANDS-ON GUY: EX-RAZORBACK JONES PLANS TO LEAVE HIS FINGERPRINTS ON THE TEAM

PROMOTERS

JERRY JONES: THE MAN WHO FIRED TOM LANDRY

He bet \$140 million he can make the Cowboys great again

Jerral W. Jones should pray that his first foray into professional sports says nothing about his second. In 1984 the Arkansas oil and gas man tried his hand as a boxing promoter. He bragged that his client—an unranked cruiser weight named Otis Bates—would become world champion. Jones assembled the largest crowd in Little Rock boxing history for Bates's first bout, assuring fans that they would witness awesome power. They did. Seconds after the fight began, Bates was knocked cold. Says Jones: "That was the end of my boxing reputation."

Now Jones is risking a lot more than his name. In March, when he bought the Dallas Cowboys football team from H.R. "Bum" Bright for a record \$140 million, he invested the bulk of his small fortune in a business with thin profit margins. Jones, 46, will have to find a way to make money fast. And that could be hard because these days the Cowboys resemble Jones's hapless boxer more than "America's Team" of yore.

'SOCKS AND JOCKS.' Last season the team won only three of 16 National Football League games. Since 1983 average home attendance has tumbled 24%, to 48,000. But the effervescent Jones waxes optimistic: "We'll win the Super

Bowl within five years." If they do, expect him to take plenty of the credit. Unlike the hands-off administration of former Cowboy owners, Jones plans to leave his fingerprints everywhere. "I want to know everything, from player contracts to socks and jocks," he says. That attitude immediately alienated General Manager Tex Schramm, who for 29 years has run the Cowboys as if he owned them. Football sources say Schramm may resign to run a new international league being organized by the NFL, forcing Jones to learn the

JONES'S GAME PLAN

His turnaround strategy for the Cowboys includes:

- Firing head coach Tom Landry and his staff; naming college chum Jimmy Johnson head coach
- Exploiting this year's No. 1 draft pick by signing a star quarterback or peddling the pick to acquire new players
- Dropping end-zone ticket price to \$19. from \$25
- Trimming costs: Cowboys lead the league in nonplaying personnel
- Seeking lucrative cable or pay-per-view TV contracts

trade more quickly than he expected.

To draw fans back to Texas Stadium, Jones needs to rebuild the team. He took what may be the first step when he fired Tom Landry, head coach for 29 seasons and hired a new staff headed by former University of Miami Coach Jimmy Johnson. Axing Landry made Jones unpopular—he even got two death threats—but hiring Johnson has excited fans. Step two is the NFL draft on Apr. 23. The Cowboys get to pick first. But the new owner muddled that process when he proclaimed that likely first-round pick Troy Aikman should take only half of his expected salary for the honor of playing in Dallas. In the end, the team may simply trade its first pick for a few sorely needed younger players.

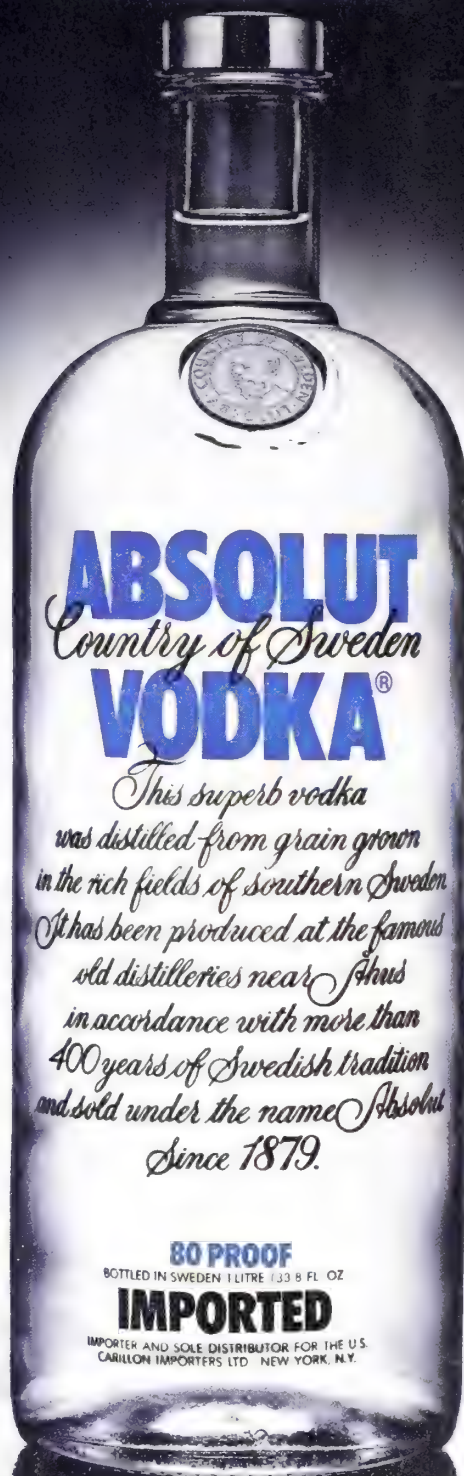
OFFENSIVE LINE. Although Jones has no franchise experience, he knows plenty about football. After growing up in Little Rock, he starred as an offensive line man and fullback at the University of Arkansas. In 1964, his roommate was none other than Jimmy Johnson. After college Jones worked at his father's insurance company until 1969, when the elder Jones sold the business and gave a big chunk of the proceeds to his son.

Flush with cash, Jones founded an oil and gas company called Arkoma Exploration Co. He sidestepped the oil bust by keeping debt low and drilling in areas with proven reserves. Throughout the mid-1980s he has bought depressed gas properties in Canada and California, planning to hold on until the market recovers. Jones is tight-lipped about the privately held company's finances, but he allows that it spends about \$24 million on drilling every year.

For recreation, Jones enjoys a highly physical brand of basketball. One contest with Johnson got so rough that Jones's wife broke into tears and stopped the game. Despite his intense love of sports, only once before has he shown interest in owning a football team. In 1966, Jones says, he arranged to raise \$5.8 million from a group of lenders to buy the San Diego Chargers. But his father felt Jones was taking on too much debt and pulled the plug. Two months later the Chargers were folded into the NFL and sold for \$11 million.

Now that he has a team, Jones clearly relishes the role of owner. Besides predicting a Super Bowl victory, he has promised a better record in 1989. Coach Johnson, he insists, is worth "five first-round draft picks and five Heisman trophies." He had better hope so. This time, with most of his money tied up in the Cowboys, Jones could be the one to take a knockout punch.

By Kevin Kelly in Dallas



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INSURANCE SHELTERS: ARE THEY WORTH THE PRICE?

Orchid farms, tuna boats, jojoba beans—the list of ways to shelter income from taxes used to be endless. Tax reform eliminated most of these creative methods, but one way remains. It's safe. It's sound. It's (stay awake) insurance. Because earnings in policies accrue tax-free, brokers and insurers are teaming up to champion a bold message: Insurance is the only tax shelter left.

At first glance, insurance products do boast the best of two worlds: growth-oriented investments in a tax-deferred shell. As part of the push, annuities, single-premium, and universal-life policies are being revamped to resemble CDs, mutual funds, and IRAs. Says Larry Carroll, a Charlotte (N.C.) financial planner: "A lot of people don't realize they're buying insurance."

They should. Despite their new investment-oriented cast, these products retain insurance costs. The tax-deferred banner hides features that bite into returns—expense fees, surrender charges, and IRS early-withdrawal penalties.

REAL ACTION. The insurance product offering the purest investment is the deferred annuity, where you invest a lump sum to be withdrawn in increments, usually after retirement. Most annuities offer a fixed rate of return, currently 8.5% to 9.5%, that's adjusted periodically by the insurer. One new twist lets investors lock in rates for a specific time period. For example, Sun Life Group's Certificate of Annuity offers "maturities" ranging from 3 to 10 years.

But the real action in annuities lies with variable prod-

ucts, whose earnings accrue at a fluctuating rate. When introduced in the early 1970s, these invested in a single equity or bond fund. But in the new crop, investors can diversify holdings among a whole family of mutual funds. For example, the nine options in Franklin Advisers' new Valuemark II annuity, issued by North American Life & Casualty, include equity funds that invest in precious metals, utilities, or real estate. The idea is to offer "options for all economic seasons," says Andrew Westhem, chairman of Western Capital Financial Services.

Admittedly, few insurance companies are known for aggressive investment expertise. That's where the use of more market-oriented managers comes in. Often, annuity funds clone existing mutual funds offered by a financial services firm, sharing the same management team, investment strategy, and holdings. For Putnam's Capital Manager, "we looked at our fund portfolio, selected five of our best-selling funds, and copied them," says Mitchell Grant, Putnam vice-president. In some cases, the strategy is tailored for the annuity.

Integrated Resources' ICap annuity offers a High Yield Fund, similar to its junk bond fund. But the annuity version is managed for both growth and income; the public fund emphasizes income.

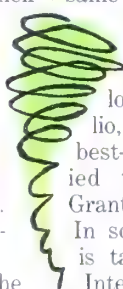
Actually, annuities may not deserve their stodgy reputation, says Rick Carey, president of Financial Planning Resources, which tracks annuity funds. In 1988, his universe of 400 funds gained 13.25% compared with 13.58% for equity funds overall. But for investors to register a real

gain, annuity funds have to outperform their public counterparts—because they labor under a double dose of costs.

First there are the insurer's mortality charges, averaging 1.4% annually, which cover the annuity's guarantee to pay back principal if the investor dies. Then there are the mutual fund's management costs, which range from 0.75% to 1.25%. With total fees running 2% to 2.5% per year, it takes at least a de-

cade for the tax-deferring component to overcome the costs and for annuities to outperform taxable investments.

The benefits of tax deferral dwindle even further when you try to get at your money. Cancel the annuity or withdraw more than 10% of your investment and you pay surrender charges: typically 6% in the first year, 5% in the second year, and so on, for six or seven years. After that you are free of the insurer—but



FEES EAT INTO THE BENEFITS OF TAX DEFERRAL

How a \$25,000 investment would grow*

	Annual fee (Percent)	Years				
		5	10	15	20	25
SINGLE PREMIUM LIFE	2.67%	\$35,167	49,469	69,587	97,888	137,697
VARIABLE ANNUITY	1.92	36,543	53,416	78,080	114,131	166,828
EQUITY MUTUAL FUND IN IRA	1.18	37,943	57,586	87,398	132,645	201,316
EQUITY MUTUAL FUND (TAXABLE, 33% BRACKET)	1.18	32,523	42,309	55,039	71,601	93,145

* Assuming 10% compounded total annual growth

DATA: INSURANCE INVESTING, FIDELITY INVESTMENTS

of the IRS. On top of regular income tax, investors are fined a tax penalty on withdrawals made before age 59½. A 40-year-old investor puts equal units in an annuity and a no-load mutual fund with equal yields.

After six years the annuity is a sheltered \$15,000; the mutual fund, taxed at 33%, is \$10,000. When he withdraws the annuity's earnings, he's a 2% surrender fee, or \$1,500; income taxes are \$1,500. Remaining: \$8,250.

This is why many financial planners do not recommend annuities for younger investors. "If you're 35 to 45 years old, the only way to get your money out is to pay big penalty—or die," says Joel Isaac-

son, head of financial planning at New York CPA firm Weber Lipschitz. One exception: an annuity used as a pension plan for a nonworking spouse. Otherwise, the best candidates are middle-age investors geared toward earning income for retirement. That's especially so for those with an inheritance, say, that's too big for an IRA, or those who can't stomach the risk in municipal bonds.

DEATH BENEFIT. The same caveats apply to single-premium life insurance, which, from an investor's standpoint, "is now virtually the same as an annuity," says Gregory Yost of Independent Financial Advisors, a Los Angeles planning firm. The two became comparable when the Technical & Miscellaneous Revenue Act of 1988 decreed that SPL "loans" would be taxable and subject to the 10% early-withdrawal penalty. SPL is also going the variable route: Monarch Life's "CaptnFlex" SPL policy offers seven funds run by Oppenheimer Management, including a zero-coupon-bond trust.

However, annual fees in SPL are higher than—sometimes double—those of annuities. The products offered by Guardian Life and Value Line Securities invest in the same funds. But Value Line's Guard II annuity's annual expenses are 1.6%; those of the Value-Plus insurance policy run from 2.5% to 3%, based on a policyholder's age and sex.

Clearly, if someone is trying to maximize retirement income, an annuity provides better yields. But SPL has advantages from an estate-planning point of view. When the policyholder dies, beneficiaries receive not only the cash buildup but the death bene-

fit—and as insurance, the money is free of income tax, unlike annuity income.

SPL, though, does not offer the world's best insurance deal. Policies tend to carry minimal coverage so that more dollars go toward building income. That's why SPL "shouldn't be your foremost means of protection," says Rudolph Watz, director of retirement plans for Value Line. "Fulfill the basic insurance needs first."

Something that can fulfill insurance needs: universal life. With these policies, premiums go toward building up the death benefit and a separate cash value, both of which accrue at the usual tax-deferred rate. Introduced by insurers 10 years ago, universal life is now being promoted by brokerages such as Merrill Lynch, PaineWebber, and Shearson Lehman Hutton, in policies repackaged to resemble retirement plans. For example, the brokers recommend annual premiums of \$2,000 (any resemblance to IRA contributions is purely intentional). Under the estimates done by PaineWebber's Provider program, a male nonsmoker starting payments at age 35 would have a cash value of \$245,345 by age 65, based on today's 8.75% return.

It sounds good. However, "if you don't need or want insurance, this could be an expensive way to save," warns Ross Nager, tax partner for Arthur Andersen in Houston. Unlike annuities and SPL, which tend to have no front-end load, these products have commissions that can equal 75% of first-year premiums.

Then there are administrative expenses and the cost of the insurance, which of course grows as the policyholder ages. "You have to hold a policy for at least 10 years before it starts to outperform term insurance and a comparable investment

like a bond fund," says Glenn Daily, insurance analyst at Seidman Financial Services.

DON'T SKIP. You may have to wait that long just to break even. Surrender charges start as high as 70%. Under Shearson's IRB program, a 35-year-old male nonsmoker who invests \$2,000 a year would have \$8,478 after four years—but could withdraw only \$5,536. It would take 13 years before he could withdraw his full account: \$41,448.

And discipline in making deposits is crucial. In an IRA, skipping a payment or two only means less money will earn interest. But suspend premiums with these programs and the cash value recedes, because it goes to maintain the death benefit. Says Robert Filderman, Shearson's insurance director: "This is not for a person unwilling to invest \$2,000 each and every year until age 65."

So for retirement savings, universal life is more restrictive than an annuity or even SPL. But since this sort of insurance still offers tax-free loans, it can be "an excellent vehicle if you have a specific goal down the road," says Douglas Fabian, publisher of the *Insurance Investing* newsletter. Proceeds from the policy could fund a college education, for example.

Even advocates of investing in insurance regard these products as supplemental to other retirement plans. First fund your IRA, your 401(k), your Keogh to the max. Then decide if tax deferral is worth the extra expenses and illiquidity. Contrary to popular belief, tax shelters haven't disappeared. But like any scarce item, they have gotten more expensive. *Troy Segal*



Smart Money

A FUND THAT LETS YOU SMILE AS THE PRIME RATE SOARS

When you watch the parade of prime rate boosts, ever wish you, too, were a bank? Pilgrim Prime Rate Trust, offered through brokers by Los Angeles' Pilgrim Group, is designed to fulfill that fantasy. Instead of stocks or bonds, this 10-month-old mutual fund buys corporate loans from big banks such as Citi and Bankers Trust, passing along most of the interest. The prime was recently raised to 11.5% from 11%, and Pilgrim is currently paying 10.9%.

That compares favorably with the current rates of 9.64% on one-year Treasury bills and the near-10% rates of many bank CDs. While Pilgrim can't hold a candle to the midteen yields of junk bond funds, the debt they hold is, by definition, speculative.

The Pilgrim yield does top that of most money market funds, but it isn't nearly as economic to acquire or as liq-

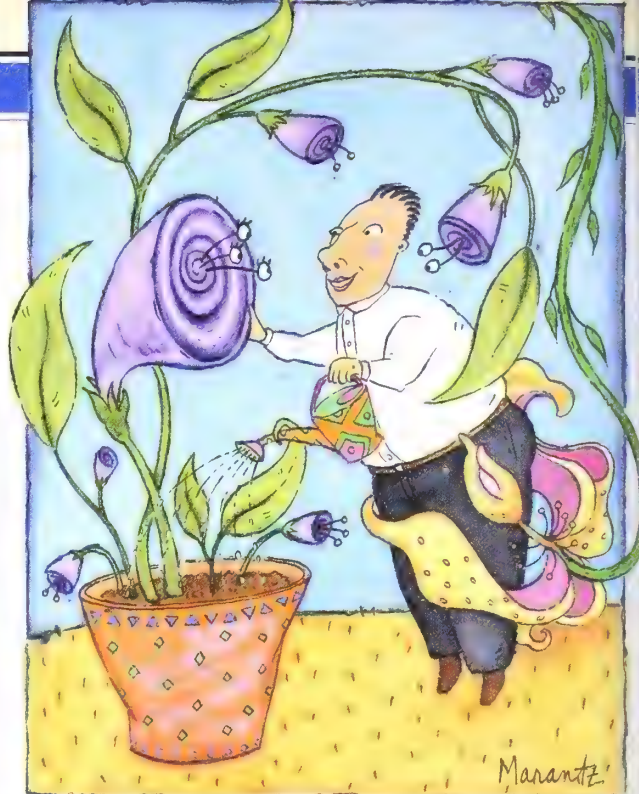
uid to hold. Just how great the risk may be is a point of much contention. Palomba Weingarten, Pilgrim's chief executive, insists the loans in which the fund invests are safe. She says the fund will only buy loans made to companies whose cash flow can be used to pay the interest and amortization and whose collateral equals or exceeds the value of the loan—companies such as Viacom, Tom's Foods, Fort Howard Paper, Payless Cashways, and Owens-Illinois.

'TRUST ME.' The fund also avoids foreign loans, loans made to single-product or high-tech companies, and loans made for real estate investments. "This is not a 'trust-me' instrument like a subordinated debenture," says Weingarten. "At no time is a lender taking a credit risk." None of the loans Pilgrim has bought are in default, the company says, compared with the 1% average default rate of commercial loans nationwide.

Still, many experts are skeptical. Roughly 70% of the loans were for mergers and acquisitions, including leveraged buyouts. In a recession, companies with high debt loads may be more susceptible to default. Given their high exposure to debt-burdened companies, Pilgrim shares are "certainly a chancy bet," says Allan Hadhazy, an analyst at *Mutual Fund Forecaster*.

With that level of risk involved, some financial advisers recommend investing in a good junk bond fund to get higher yields with about the same default risk. Another advantage of a junk bond mutual fund: Should the market begin to turn against you, your shares are quickly redeemable, not frozen like Pilgrim's.

Laura Zinn



Gardening

THESE SEED CATALOGS GO BEYOND THE GARDEN VARIETY

When you can't walk through a hardware store without bumping into racks of seed packets, you know it's spring. But if you're tired of those familiar flower faces, you may be ready for the more exotic botanical delights available through catalogs.

For a wide range of backyard vegetables and flowers, old standbys like W. Atlee Burpee's catalog can't be beat. But hundreds of lesser-known catalogs offer pleasant surprises that are just as easy to grow. Many of them carry old-time varieties that produce seeds gardeners can collect for next year. These may not bear as abundantly as some modern hybrids do, but the fruits and vegetables often retain that indescribable taste your grandfather remembers.

REGIONAL TASTES. Some companies specialize in varieties especially suited to your region. Johnny's Selected Seeds in Albion, Me., for example, sells early maturing melons and hardy tomatoes for northern gardeners.

Edible flowers such as nasturtiums, the rage in nouvelle cuisine, are available from Shepherd's Garden Seeds in Felton, Calif. Some of the company's nine varieties of basil smell of cinnamon anise. California's Redwood City Seed Co., a chili specialist, sells what it claims is the world's hottest pepper, a pea-size scorch 30 times hotter than the jalapeño.

For tomatoes, choose from 300 varieties supplied by Tomato Seed Co. in Metuchen, N.J. For Asian vegetables, such as bitter melon, prize for its distinctive tart taste, there's Tsang & Ma International in Belmont, Calif.

A handy guide to all but the most obscure catalogs is Hal Morgan's *The Mail Order Gardener* (Harper & Row, \$12.95). Kent Whealy's *The Garden Seed Inventory* (Seed Savers Publications, Rural Route 3, Box 239, Decorah, Iowa 52101, \$17.50) lists 300 sources for 5,000 kinds of seeds; all are older varieties handed down for generations.

Rob Ho

Some experts question the safety of Pilgrim's loans

uid to hold. The fund imposes a front-end load of almost 3% above the price per share, now \$10. As with a CD, there is a penalty for early withdrawal, equal to 90 days' interest for shares held less than a year.

While Pilgrim's shares are offered continuously, you can sell your shares back to the fund on only one day each quarter. The price is set at \$10, or 31¢ less than you paid for them. Pilgrim's minimum initial investment is \$5,000, or \$2,000 for IRAs.

The main concern about Pilgrim, though, is the de-



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What's In

ZOOS WITH CREATURE COMFORTS

In the sweltering heat, a velvety black-and-blue bird flits past your face to sip from a waterfall splashing toward a pool of piranha, as alligators linger nearby...

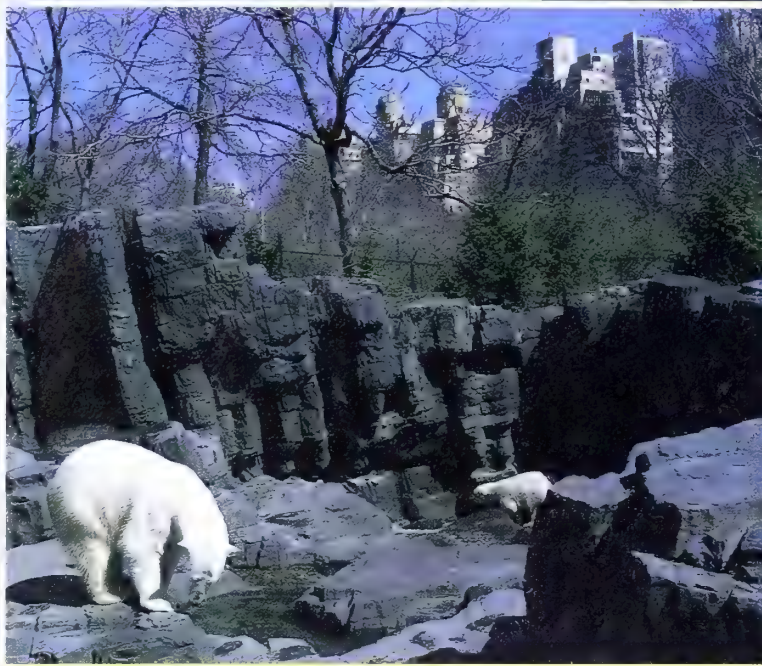
No, you aren't on a trek through the Amazon jungle or inside a Disneyland pavilion. You're at a local zoo—New York's refurbished Central Park Zoo, in this case—viewing a new type of exhibit fast becoming the norm throughout the country.

Gone are the prisonlike cells with their pacing lion or slumbering raccoons. Now you wander through "environments," where different creatures dwell compatibly in replicas of their natural habitats. Fine wires or sheets of glass separate animals and



humans and let you come virtually eyeball-to-eyeball with a polar bear, seal, or python.

Central Park's facility epitomizes the new zoos—compact



■ **SETTING FREE THE BEARS: A NATURAL HABITAT IN CENTRAL PARK'S NEW ZOO**

enough to be located near midtown hotels and toured in a short time. The year-old Indianapolis Zoo (317 638-8072) houses some 2,000 creatures in 64 acres of man-made deserts, plains, forests, and seas just a few blocks from the city's center. And the 102-year-old Washington Park Zoo in Portland, Ore. (503 226-1561), has been thoroughly rebuilt as a naturalistic home for 500 animals.

NO SHOWS. Unlike the 186-acre Arizona-

Sonora Desert Museum near Tucson or the 265-acre Bronx Zoo, the new zoos don't aim to be encyclopedic. Kids won't find a real Ba-

bar at the tiny Central Park Zoo: Its pachyderms were packed off to make room for a rain forest with towering plants and tropical birds. And visitors to the new Portland zoo who expect beasts like those in *Gorillas in the Mist* must settle for only chimps and orangutans.

Gone, too, are the once traditional shows with juggling seals and skating chimps. Instead, families enjoy adventurous endeavors. In the Central Park Zoo's education program (212 439-6538), instructors send groups into the rain forest on a naturalist's scavenger hunt to spot exotic flora and fauna. At other zoos, trainers in scuba gear show how dolphins learn to



■ **HOO ARE YOU: AN OWL IN PORTLAND'S ZOO**

■ **PORTLAND PACHYDERM, BIG APPLE APES: LITTLE ZOOS STICK TO LITTLE ANIMALS**

day-night lighting lets you see bats fly in a cave-like setting.

Opening this spring: an Africa zone at the zoo in Portland, with hippos, zebra, and impala at a watering hole; a Indianapolis Zoo pavilion providing views of whales from above and below the water and the Los Angeles Zoo Adventure Island, where children can pet newborns in nursery. A similar children's area at Lincoln Park Zoo in Chicago has a kitchen where chefs prepare to feed animals such delicacies as "Armadillo's Surprise" (sweet potatoe grated eggs, and meal worm) and "Tarantula's Treat" (crickets sprinkled with calcium).

Don Dun



Worth Noting

■ **YIELD REVEALED.** CPAS Laventhol & Horwath have a formula for finding the taxable yield you'd need to match that on a tax-free muni: Divide the muni yield

by 1 minus your tax bracket as a decimal. Say you're in the 33% bracket and eyeing a 7% muni. Take 1-0.33. Divide that 0.67 into 7. Result: You'd need a 10.45% taxable bond to net you as much.

■ **AMERICAN ORIGINAL.** The 100th birthday of artist

Thomas Hart Benton is being commemorated with a major touring exhibit. Through June 18 it will be at the Nelson-Atkins Museum in Kansas City, Mo. The show will also visit New York's Whitney Museum and the Detroit Institute of Arts.

■ **STAY 'N' SAVE.** Forget rental cars and room upgrades—guests at Stouffer hotels earn U.S. Savings Bonds. The awards go from a \$50 bond for three nights to \$1,000 for 50 nights, and stays need not be consecutive. Call 800 468-3571.

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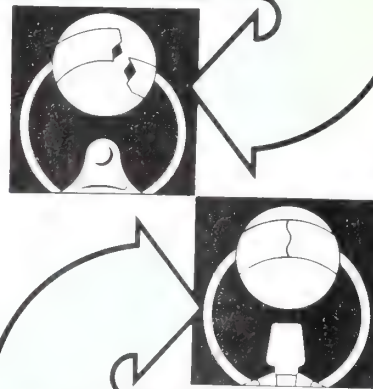
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We built the best track record in the industry by demanding a lot more from our products than you ever will. OKIDATA engineers call this "championship specs." Over 3 million OKIDATA users call it rugged reliability. And it shows in the quality and performance of every printer and modem we make.

You can see it in our new 300 series of 9-pin and 24-pin printers. Their speed, print quality and sheer versatility can carry a ton of paperwork. With day in, day out reliability. OKIDATA wouldn't have it any other way. Why should you?

Call 1-800-OKIDATA for the dealer near you.

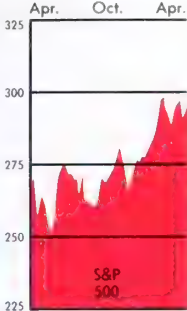
OKIDATA[®]
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Investment Figures of the Week

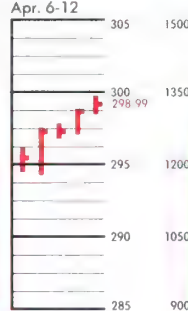
STOCKS

meandered gently upward
ers exhibited no great en-
n. The Dow rose a mere
its as traders awaited re-
f producer price index and
ales numbers. Bright spots
d chemical and technology
which showed strength late
week. Bonds were as listless
ties, with long-term rates
up and short-term rates
down. Overseas bourses
ackluster week, with Lon-
d Tokyo recording declines.

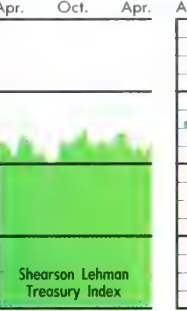
STOCKS



BONDS



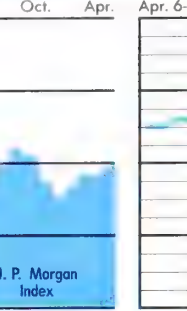
THE DOLLAR



STOCKS



BONDS



THE DOLLAR



MARKET ANALYSIS

STOCKS	Latest	% change Week	% change 52-week
DOW JONES INDUSTRIALS	2319.65	0.6	10.1
COMPANIES (Russell 1000)	158.28	0.9	10.3
COMPANIES (Russell 2000)	161.21	1.7	11.0
COMPANIES (Russell 3000)	170.16	1.0	10.3

FOREIGN STOCKS	Latest	% change (local currency) Week	% change (local currency) 52-week
DOW JONES (FINANCIAL TIMES 100)	2033.0	-2.2	12.3
NIKKEI INDEX	33,256.5	-0.3	23.2
TOYO INDEX (TSE COMPOSITE)	3568.6	0.4	5.0

FUNDAMENTALS	Latest	Week ago	Year ago
90-DAY TREASURY BILL YIELD	9.0%	9.1%	6.0%
30-YEAR TREASURY BOND YIELD	9.1%	9.0%	8.8%
S&P 500 DIVIDEND YIELD	3.6%	3.5%	3.4%
S&P 500 PRICE/EARNINGS RATIO	12.0	11.9	15.3

TECHNICAL INDICATORS	Latest	Week ago	Reading
S&P 500 26-week moving average	284.1	283.3	Positive
Stocks above 26-week moving average	60.6%	58.4%	Neutral
Speculative sentiment: Put/call ratio	0.21	0.21	Negative
Insider sentiment: Vickers sell/buy ratio	1.36	1.36	Positive

INDUSTRY GROUPS

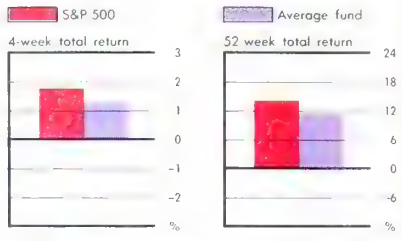
4-WEEK LEADERS	% change 4-week	% change 52-week	Strongest stock in group	% change 4-week	% change 52-week	Price
ALUMINUM	11.1	21.0	WESTMORELAND COAL	22.7	-0.6	19 7/8
REBUILDING	9.2	31.5	PHM	30.2	89.8	14
KEY CENTER BANKS	9.1	37.0	CHEMICAL BANKING	15.5	51.3	35 3/8
UTION CONTROL	7.4	22.1	WASTE MANAGEMENT	9.6	35.0	47 1/4
INES	7.1	38.8	NWA	34.7	100.0	88 3/4

4-WEEK LAGGARDS	% change 4-week	% change 52-week	Weakest stock in group	% change 4-week	% change 52-week	Price
OMOBILES	-6.8	3.4	FORD MOTOR	-7.6	1.3	47 1/4
LTH CARE SERVICES	-5.8	-35.9	GENENTECH	-11.5	-53.4	17 3/8
DWARE AND TOOLS	-5.0	-1.6	BLACK & DECKER	-21.3	-7.5	18 1/2
KERAGE FIRMS	-4.9	20.6	MORGAN STANLEY	-12.4	39.7	60 3/4
NSPORTATION SERVICES	-4.5	-17.3	FEDERAL EXPRESS	-8.6	-7.4	45 1/4

MUTUAL FUNDS

LEADERS	Week total return	%	LAGGARDS	Four-week total return	%
IL & BEAR SPECIAL EQUITIES	8.2		STRATEGIC GOLD/MINERALS	-7.2	
ANCIAL STRATEGIC HEALTH SCIENCES	6.9		SHEARSON LEHMAN HUTTON PRECIOUS METALS	-6.4	
I. GLOBAL GROWTH—JAPAN	6.2		VAN ECK GOLD/RESOURCES	-6.0	

Week total return	%	52-week total return	%
JFMANN	61.4	STRATEGIC GOLD/MINERALS	-23.1
ITEL CAPITAL APPRECIATION	33.6	STRATEGIC INVESTMENTS	-19.1
UMBIA SPECIAL	33.4	STEADMAN OCEANOGRAPHIC TECHNOLOGY	-16.4



RELATIVE PORTFOLIOS

Amounts sent the present of \$10,000 held one year	Foreign stocks	U. S. stocks	Money market fund	Treasury bonds	Gold
Changes indicate total returns	\$12,204 -1.88%	\$11,297 +1.08%	\$10,662 +0.16%	\$10,566 -0.84%	\$8,567 -0.43%

on this page are as of market close Wednesday, Apr. 12, 1989, unless otherwise indicated. groups include S&P 500 companies only; performance and share prices are as of market close Apr. 11. Mutual fund returns are as of Apr. 7. Relative portfolios are valued as of Apr. 11. A more detailed explanation of this page is available on request.

DON'T LET THE U.S. BECOME ONE BIG CASINO

Legalized gambling, in its multifarious forms, is expanding rapidly. There are several reasons. For one, new gambling technologies are making games easier and more exciting to play, and more accessible. But equally important is the aura of legitimacy about gambling that has been carefully fostered by the nature of the folks now peddling the games: state governments and blue-chip leisure-and-entertainment conglomerates.

It would be foolish and unnecessary to prohibit gambling, but there are some serious problems with it. One is the role of the states as lottery promoters. States are spending \$200 million a year advertising lotteries. Think about how we would feel if the state not only sold liquor but advertised it on TV. There is also a conflict of interest: The state is both running games and regulating them.

A problem that extends far beyond the state lottery is the sheer volume of high-pressure hype that attends the gambling boom in all its forms. Gambling is unusually susceptible to stimulation by advertising—as well as to the availability of gambling opportunities and the allure of a game's design. (The new technology is making games, notably video poker, extraordinarily seductive.) The net effect, then, of all the hype, the proliferation of gambling outlets, and glitzy new games has been to cajole people into betting bigger bucks than they otherwise would. Many of those cajoled are the low-income people least able to afford gambling.

While gambling should remain legal, something needs to be done to rein in Americans' propensity to gallop after something for nothing. The states should remove themselves from the lottery business. If they insist on raising money through lotteries, let them issue licenses to private vendors, just as states license liquor stores. State politicians are attracted to lotteries because every dollar raised is one dollar that the state doesn't have to raise through taxes. But lotteries don't produce a huge amount of money for state treasuries—less than 5% of the budgets. And something must be done about the hype. We control liquor and cigarette advertising; let's control gambling advertising, too. The British model makes sense: It accommodates demand for gambling without stimulating it.

CONGRESS SHOULD STOP PAMPERING ESOPs

Employee stock ownership plans—an idea that has been around for 35 years—are suddenly the rage among big corporations. In recent days, NWA, Lockheed, and Tribune all have said they may establish ESOPs. Experts speculate that plenty of others are also considering them.

Why the new appeal for such an old idea? It seems to have little to do with the purpose of ESOPs, which is to widen stock ownership by employees. That, of course, is a good

idea, especially since productivity may be increased by more highly motivated worker-owners. Instead, ESOPs have arrived because they're a prime takeover defense tool. The reason: A Delaware court has reaffirmed a decision upholding Polaroid Corp.'s placing enough shares into an ESOP to block a bid from Shamrock Holdings PLC. Delaware's takeover statute requires that raiders acquire 85% of the outstanding stock when they make a hostile tender offer, and it's the state where many companies are incorporated.

That would be fine, except that Washington subsidizes ESOPs with tax breaks that already cost \$400 million in revenues every year. Lawmakers thought ESOPs should be subsidized because of the built-in incentive of employee ownership. But the productivity effect is more likely to show up if workers are involved in decision-making. So using ESOPs solely as a management entrenchment device—essentially as a shark repellent—has nothing to do with the lawmakers' intent and casts doubt on the validity of a federal subsidy.

There are still many who question the social value of ESOPs—and the breaks Congress has given them. Using ESOPs as shark repellents merely strengthens the argument of opponents. It may be time to change the law so that genuine worker participation is required if ESOPs are to retain their favored tax status.

ARE THE THRIFTS GETTING ANOTHER EASY RIDE?

As Congress designs its massive bailout of the savings and loan insurance fund, it should keep one principle firmly in mind: The least that taxpayers deserve for pumping \$150 billion into a cesspool created by the thrift industry should be the assurance that quick-buck operators never get another chance to pick their pockets.

Sadly, the House Banking Committee bowed to the arguments of the still-powerful savings and loan lobby and staged a massive retreat from that principle on Apr. 11. The panel voted tentatively to scrap President Bush's recommendation that insured thrifts be required by 1991 to have capital equal to 6% of their assets. That would put thrifts on the same level as banks. Instead, the committee approved an amendment that would allow thrifts to average just 3% capital. The capital requirement would be based on a sliding scale, depending on the riskiness of the loan.

Caving in to the industry in this fashion could undermine the goal of shoring up thrifts once and for all. A major reason that the S&L crisis spun out of control is that many thrift owners had virtually no equity invested in their institutions. They were thus able to take wild risks with other people's money. Now these bad bets must be covered by the public at large. The committee even considered weakening the definition of capital, but fortunately pulled back from that dilution.

The Treasury Dept. warns that Bush will veto the bill if it reaches his desk with weakened capital provisions. The President should stick to his threat—and, if Congress fails to act responsibly on the first try, he should make the lawmakers do it again until they get it right.

